

**Internal Revenue Service
APPEALS OFFICE**

Number: 201036031
Release Date: 9/10/2010

Date: June 18, 2010

**ORG
C/O
ADDRESS
CITY STATE**

UIL: 501.03-30

Department of the Treasury

Person to Contact:

Employee ID Number:

Tel:

Fax:

Contact Hours: 8:00 to 4:30

Refer Reply to:

AP:FE:

In.Re:

EO Revocation

EIN:

Form Required to be Filed:

1120

Tax Periods Ended:

12/20XX, 12/20XX & 12/20XX

Dear :

This is a final adverse determination as to your exempt status under section 501(c)(3) of the Internal Revenue Code (IRC). It is determined that you do not qualify as exempt from Federal income tax under IRC Section 501(c)(3) effective February 13, 2002.

Our adverse determination was made for the following reasons:

You are not operated exclusively for charitable, educational, or other exempt purposes. More than an insubstantial part of your activities were in furtherance of a non-exempt purpose and you were operated for the purpose of serving a private benefit rather than public interests. Part of your earnings inured to or were for the private benefit of individuals or other non-exempt organizations. Further, no exempt purpose activities are described on the Form 990 filed for 20 .

Contributions to your organization are not deductible under Code section 170.

You are required to file Federal income tax returns on the form indicated above. You should file these returns within 30 days from the date of this letter, unless a request for an extension of time is granted. File the returns in accordance with their instructions, and do not send them to this office. Processing of income tax returns and assessment of any taxes due will not be delayed because you have filed a petition for declaratory judgment under Code section 7428.

If you decide to contest this determination under the declaratory judgment provisions of Code section 7428, a petition to the United States Tax Court, the United States Court of Claims, or the district court of the United States for the District of Columbia must be filed within 90 days from the date this determination was mailed to you. Contact the clerk of

the appropriate court for rules for filing petitions for declaratory judgment. To secure a petition form from the United States Tax Court, write to the United States Tax Court, 400 Second Street, N.W., Washington, D.C. 20217.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

You also have the right to contact the Office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal Appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free, 1-877-777-4778, and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

Taxpayer Advocate Service

CITY STATE

Phone: ()

See the enclosed Notice 1214, Helpful Contacts for Your "Notice of Deficiency" for additional Taxpayer Advocate telephone numbers and addresses.

Sincerely,

Karen A Skinder
Appeals Team Manager

Enclosures:

Notice 1214 Helpful Contacts for your 'Deficiency Notice'

cc: .



DEPARTMENT OF THE TREASURY
Internal Revenue Service
8701 S. Gessner, M/S 4900HAL
Houston, TX 77074-2926

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

July 17, 20XX

ORG
ADDRESS

Taxpayer Identification Number:
Form:
Tax Year(s) Ended:
Person to Contact/ID Number:
Contact Numbers:
Telephone:
Fax:

Certified Mail - Return Receipt Requested

Dear _____ :

We have enclosed a copy of our report of examination explaining why we believe revocation of your exempt status under section 501(c)(3) of the Internal Revenue Code (Code) is necessary.

If you accept our findings, take no further action. We will issue a final revocation letter.

If you do not agree with our proposed revocation, you must submit to us a written request for Appeals Office consideration within 30 days from the date of this letter to protest our decision. Your protest should include a statement of the facts, the applicable law, and arguments in support of your position.

An Appeals officer will review your case. The Appeals office is independent of the Director, EO Examinations. The Appeals Office resolves most disputes informally and promptly. The enclosed Publication 3498, *The Examination Process*, and Publication 892, *Exempt Organizations Appeal Procedures for Unagreed issues*, explain how to appeal an Internal Revenue Service (IRS) decision. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process.

You may also request that we refer this matter for technical advice as explained in Publication 892. If we issue a determination letter to you based on technical advice, no further administrative appeal is available to you within the IRS regarding the issue that was the subject of the technical advice.

Letter 3618 (04-2002)

If we do not hear from you within 30 days from the date of this letter, we will process your case based on the recommendations shown in the report of examination. If you do not protest this proposed determination within 30 days from the date of this letter, the IRS will consider it to be a failure to exhaust your available administrative remedies. Section 7428(b)(2) of the Code provides, in part: "A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted its administrative remedies within the Internal Revenue Service." We will then issue a final revocation letter. We will also notify the appropriate state officials of the revocation in accordance with section 6104(c) of the Code.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,

Marsha A. Ramirez
Director, EO Examinations

Enclosures:
Publication 892
Publication 3498
Report of Examination

Letter 3618 (04-2002)
Catalog Number 34809F

Form 886-A REV JANUARY 19XX	EXPLANATION OF ITEMS	07/17/20XX Page 1 of 66
NAME OF TAXPAYER ORG	TAX IDENTIFICATION NUMBER	YEAR/PERIOD ENDED 12/31/20XX — 12/31/20XX

LEGEND

ORG = Organization name XX = Date Address = address City =
city State = state Country - country wife = wife M-IRA = M-
IRA A-Dean = A-Dean website = website Product = product IRA
= IRA Number = number POA = POA GE-1 = 1st GE RAA-1 & RSA-2
= 1st & 2nd RSA BM-1 & BM-2 = 1st & 2nd BM FAC-1, FAC-2 & FAC-3 = 1st,
2nd & 3rd FSA Dean-1 & Dean -2 = 1st & 2nd Dean ED-1 = ED-1 AAS =
AA ATTN-1, ATTN-2, ATTN-3, ATTN-4 & ATTN-5 = 1st, 2nd, 3rd, 4th & 5th
ATTORNEYS DIR-1, DIR-2, DIR-3, DIR-4, DIR-5 & DIR-6 = 1st, 2nd, 3rd, 4th
5th & 6th DIRECTORS RA-1 THRU RA-41 = 1st THRU 41st RELATED ASSOCIATE
CO-1 THRU CO-64 = 1st THRU 64th COMPANIES:

ISSUES:

ORG failed to operate as an organization exempt under Section 501(c)(3) of the Internal Revenue Code.

Payments made to or for the benefit of President/Director DIR-1 constitute direct or indirect private benefit/inurement.

Payment made to family members of President/Director DIR-1 constitutes private benefit/inurement.

ORG failed to file employment tax returns.

ORG failed to accurately prepare Form 990, Return of Organization Exempt from Income, for the tax years ending December 31, 20XX through tax year ending December 31, 20XX.

FACTS:

ORG (herein referred to as "ORG") was incorporated on February 13, 20XX and received a certificate of incorporation from the State Secretary of State as a Domestic Non-Profit Corporation. The initial Articles of Incorporation filed with State Secretary of State was a fill-in form and ORG checked the box which stated the corporation was formed for the purpose of "Engaging in any lawful activity for which corporations may be formed under Chapter 2, Title 12, of the State Revised Statutes (Non-Profit Corporation Law)."

On February 3, 20XX, ORG filed amendments to the Articles of Incorporation and this document provided that "the corporation shall be operated exclusively for charitable, religious, educational and/or scientific purposes under 501(c)(3) of the Internal Revenue Code."

ORG filed Form 1023, Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code, on April 10, 20XX.

Part II of Form 1023, Part II, "Activities and Operation Information" states:

The ORG ("Foundation ") will operate exclusively for educational and charitable purposes. In particular, the Foundation will provide CO-1 ("CO-1") LL.M programs in Tax and Human Rights with contributions in order that the programs will be able to provide support to their students. The Foundation is viewed as an integral fundraising activity required by the LL.M programs in order to continue their success.

The CO-1 accredited by the American Bar Association, American Association of Law Schools, and Southern Association of Colleges and Schools. The CO-1 was founded under the Archdiocese of City in 19XX. The LL.M program in Tax was founded residentially in 19XX and founded online in 19XX. The Human Rights LL.M program was founded in 20XX.

The Foundation will hold conferences, meetings, and assemblies to provide a forum for the discussion and dissemination of relevant information and data to promote a better understanding of international, economic, tax and fiscal topics. The Foundation will sponsor at least three conferences each year at CO-1 featuring such economic and fiscal topics.

The Foundation will edit and publish papers, magazines, pamphlets, periodicals and books.

ORG's bylaws state the purposes of ORG "are promoted through an educational program directed towards tax professionals, international law students, and educational programs; are developed through conferences, committees, projects and programs...."

The bylaws state that ORG is established as "exclusively charitable" and listed the following:

- a) To promote education within the field of tax, finance, and economics;*
 - b) To promote the standards of professional tax practices;*
 - c) To promote the study of international law;*
 - d) To promote education at any level;*
 - e) To provide charitable assistance to the LL.M in International Taxation and Offshore Financial Centers or LL.M in Intercultural Human Rights at CO-1, City in the state of State, or any other educational institution.*
- fi It is expressly authorized and contemplated that the Corporation, may and will, engage in an active profit making business consistent with the Charitable Mission, and may and will engage in any other active profit making business that is not inconsistent with the Charitable Mission, but only to an insubstantial extent and shall have all the necessary powers to fulfill these objectives;*
- g) This Corporation may solicit and accept gifts, grants, and contributions from the general public, private and public charitable organizations, and various public and governmental agencies, and to distribute the same to such public and governmental agencies as the Directors deem appropriate. It may acquire by purchase or gift, such property whether real or personal to facilitate its charitable mission and to have and exercise all powers, rights and privileges granted by the government of State.*

ORG was granted exemption from Federal income tax under Section 501(c)(3) of the Internal Revenue Code on May 10, 20XX as a organization exempt under IRC §509(a)(1) and §170(b)(1)(A)(vi). The application was timely filed within 15 months from when the organization was created or formed.

ORG's maintained their records on a cash basis. ORG's accounting period ends December 31st. Filing information for the Form 990s is as follows:

20XX — Filed on November 18, 20XX

20XX — Filed on December 13, 20XX — filed late due to

20XX — Filed on October 17, 20XX – filed late due to

20XX – Not filed as of July 2, 20XX

20XX — Not filed as of July 2, 20XX

ORG's address of record, as reflected on Form 990 for 20XX and 20XX, was Address, City, State. During the audit, ORG provided testimony that this address was the register agent's office in City. Per ORG, the laws of the State of State require non-profit corporations have an office in the state of State. The registered agent in the audit years, RA-1, is not an officer, director or employee of ORG and was not involved with ORG other than serving as the designated registered agent.

ORG's current address of record, as reflected on Form 990 for 20XX, is Address, City, State.

Per the filed Form 990s (20XX through 20XX), the directors and officers of ORG are as follows:

- DIR-1 (herein referred to as "DIR-1"), City, State — President²
- DIR-2³ (herein referred to as "DIR-2") — City, State — Director

President DIR-1 directed the activities relating to ORG from his office at CO-1 and used CO-1's address (Address, City, State) on various ORG documents. DIR-1' was the full-time director of the LL.M. in International Tax Program at CO-1, City, State.

The LL.M. program at CO-1 is an on-line program whose curriculum includes courses in five concentration areas: Offshore Financial Centers, US tax, Anti-Money Laundering & Compliance; E-Commerce; and Trust and Corporate Administration & Compliance. The program focuses on the global tax aspects of compliance and planning for both individuals and corporations. The courses have been designed to prepare the practitioner to identify issues, perform research, use problem-solving skills, and provide planning advice.

DIR-1 holds a degree in Political Economics of the law track of the CO-2 and a Juris Doctorate form CO-3 CO-1. His LL.M., specialized in European Business and Taxation, is from the CO-4.

¹ Per the State Secretary of State records, DIR-1 was the registered agent from February 13, 20XX until RA-2

was appointed on April 7, 20XX. RA-2 is discussed later in this report.

2 DIR-1 uses the title "President" and "Co-Director" on various documents submitted for the examination. DIR-2's name was misspelled as "DIR-2" on the 20XX, 20XX and 20XX Form 990s.

DIR-2 is Co-Director of the CO-5 and University Law Librarian of the CO-5. DIR-2 holds Masters Degrees from the CO-7 and CO-8, a Juris Doctor from the CO-9, and a Ph.D. from the University of State. DIR-2, although designated as the director of ORG, in an interview said he provided no day-to-day oversight. He did attend Board of Director meetings both face-to-face and telephonically.

DIR-1, as president of ORG, has submitted Form 2848, Power of Attorney and Declaration of Representative, to change the representation of ORG before the Service on three occasions. In addition, DIR-1 signed a one-day authorization for RA-3 to allow RA-3 to represent ORG in a deposition held on February 7, 20XX.

An examination of ORG's Forms 990 for the tax periods ending December 31, 20XX, December 31, 20XX and December 31, 20XX were conducted. The initial contact with ORG's representative, RA-4, was on May 5, 20XX. The examination was begun based on a referral from the Large and Midsize Business (LMSB) Division. The referral indicated that the organization could be an accommodating charity for tax shelter purposes pursuant to Notice 20XX-81 issued by the Service on December 4, 20XX. (EXHIBIT A)

Per the notice, the Internal Revenue Service and the Treasury Department are aware of a type of transaction in which a taxpayer claims a loss upon the assignment of a section 1256 contract to a charity but fails to report the recognition of gain when the taxpayer's obligation under an offsetting non-section 1256 contract terminates.

This notice alerts taxpayers and their representatives that these transactions are tax avoidance transactions and identifies these transactions, and those that are substantially similar to these transactions, as listed transactions for purposes of § 1.6011-4(b)(2) of the Income Tax Regulations and §§ 301.6111-2(b)(2) and 301.6112-1(b)(2) of the Procedure and Administration Regulations. This notice also alerts parties involved with these transactions of certain responsibilities that may arise from their involvement with these transactions. ORG received assignment agreements to which the notice applied during the tax years ending December 31, 20XX and December 31, 20XX.

Information provided from LMSB indicated that the promoter of the Notice 20XX-81 transactions was an organization called the CO-10 (including CO-10 and other CO-10 subsidiary/affiliate). Based on the information reviewed, CO-10 made no serious attempt to eliminate any semblance of a U.S. presence until sometime between midyear 20XX and the beginning of 20XX. This was the same time period in which they were representing themselves as the owner of the Notice 20XX-81 promotion. Although CO-10's website currently directs all U.S. clients to their City office, available information indicates U.S. activities were conducted through DIR-1 and his offices CO-1. This included the following:

1) DIR-1 Work with CO-10

Per the CO-10 in existence at 20XX, CO-10 was "established to publish relevant technical works." It stated that later in the year CO-10, in association with CO-11, was to have published the definitive encyclopedia of company and trust legislation. The general editors were to be GE-1 (chairman of the CO-10) and DIR-1. The work was to contain the complete company and trust legislation from all major offshore and onshore financial centers for use in tax planning, together with commentary and relevant cases. They also planned to publish (through CO-11) a comprehensive electronic and paper reference work on e-commerce law and taxation. An abbreviated version for the businessman and consumer, with a more extensive version aimed at the practitioner, would be available.

2) CO-10 Reports & Web Site U.S. Contact Info

A summary of U.S. contact information posted since 19XX in the CO-10 web site and editions of the CO-10 Report shows that DIR-1 was the CO-10 agent within the U.S. during this whole time and that at least until 12/XX CO-10 listed a U.S. contact (DIR-1) separate from CO-10.

Issue #11 of the CO-10 Report (estimated to have been published in March, 20XX) contains comments regarding the March U.S. Treasury disclosure initiative to combat abusive tax avoidance transactions. It states that *"Tax planning for US residents and nationals is becoming increasingly difficult as more of the existing tax breaks and loopholes are closed. However, CO-10 has great expertise in international tax planning for US nationals and residents. We have a specialist tax planning department based in City under the direction of DIR-1 as well as other experts within the CO-10 who can advise on American tax issues."*

Near the back of each CO-10 Report there is an additional information listing. It depicts each CO-10 office location, the office contact, e-mail address, and phone numbers. Either there has not been an issue of the Report since 8/XX or they are not available on the web site.

TABLE DELETED

With the 11th issue of the CO-10 Report, CO-10 was also listed and it reflected the phone and fax numbers previously shown for CO-10 COUNTRY. The CO-10 COUNTRY phone and fax numbers were different, but still with a City area code. Issue 15 only shows CO-10, with the contact person being RA-5, another CO-10 manager. Issue 16 returns to the previous format of separate listings for CO-10 COUNTRY and CO-10, with DIR-1 as the contact for both. Beginning with issue 20 (dated 5/XX) the US listing is combined, showing United States of America: CO-10 and then DIR-1.

A CO-10 showing a 19XX – 20XX copyright and containing information on events occurring as late as mid 20XX shows CO-10, Ltd. as having a U.S. presence, providing the CO-1 L.L.M. CO-12 building as its U.S. contact address. It also lists DIR-1 as "Principal Staff" and the offices' "specialist services" as Tax Practitioners. The e-mail address posted is website.

Another version of the CO-10, which was printed sometime after 4/18/XX (page 17 cites an

event having taken place on that date), shows under the CO-10 Directory section both an office in the U.S. at ADDRESS, CITY, STATE and a separate listing for CO-10 at the CO-1 CO-12 Building.

The directory in another CO-10 Report, as well as on the web site when downloaded on 3/21/XX, also has two U.S. entries. The first listing names CO-10 (the entity that promoted the Notice 20XX-81 transactions) and instructions to contact DIR-1. No physical address is shown and the contact numbers are the same as in previous U.S. listings. The second listing for CO-10 provides the same CO-1 address and phone numbers, but does not include a contact name.

3) Documentary Evidence of DIR-1 Marketing for CO-10

During the examination of ORG Form 990s, some documents were provided by ORG and some documents were provided by third party contact documenting the activity of DIR-1 as independent developer and market of tax products and a representative of CO-10 through his office at CO-1. Specific items include:

- A prototype generic e-mail attachment dated 2/13/XX from DIR-1 to "US CLIENT". The attachment showed its source as CO-10 (CO-10) with the CO-1 address and phone numbers and DIR-1 e-mail address at CO-10. The topic was "Tax Efficient Strategies" and basically outlined "three of our tax efficient products", the same types of entities CO-10 markets in all its literature; insurance structures, non-profit/offshore structures and hybrid company structures. It also lists the tax advantages and possible disadvantages of each. It states they have a legal opinion from U.S. lawyers advising that correctly structured and managed hybrid companies are not required to report their membership interests in the US. Such an opinion specifically addressed to each client can be arranged for a one time fee of \$. It also states that CO-10 is a one-source solution for offshore planning, offering offshore private banking and investment services. The attachment ends with DIR-1 requesting to talk again this week by telephone.
- A detailed description of the CO-10 hybrid company and how by using tailor designed arrangements, guarantee members neither own shares nor have control, so that anti-avoidance legislation is ineffective in taxing profits rolled up within a hybrid structure. *"Additionally, it will normally be the case that such a structure does not bring about any reporting requirement for the Guarantee members so, on a practical level, unwanted attention is avoided."* It then discusses the same services and fees CO-10 details in its web site that would give the appearance of legitimacy to the structure.
- A copy of a CO-10 Master Card application cover letter from a RA-6 in City sent to CO-10 Country). The letter copy was faxed to DIR-1 at CO-1 on 3/19/XX. The cover letter stated he was a personal and business friend of DIR-1 who recommended that he do this. He wanted wire instructions ASAP to send funds.
- An E-mail from DIR-1 to "RSA-1 and RSA-2" dated 4/16/XX regarding CO-10 Country sent with a copy to website. DIR-1 had spoken to RSA-2 about the "principal

company" contemplating the services of RSA-1 as its "RSA" broker. It appears that "RSA-1" is preparing to act as a broker in setting up and maintaining trading accounts for foreign principal companies through "CO-13" (CO-13) or another bank. There was a question on how to set this up. DIR-1 states that the principal could have the account set up through BM-1/BM-2 in less than an hour. He said *"I think BM-2 is in the best position to know what CO-13 needs though either RSA-2 or myself can do this, or the local CO-10 office"*. He further stated *"my concern for the foreign principal having a local RSA account is the possibility of attracting RSA taxation to the income produced from trades. I have not looked into this but will if I am so instructed"*.

- Either a partial or complete DIR-1 resume consisting of his association and work for various CO-10 divisions, a listing of published works and presentations, and education. He indicated work done for CO-10, CO-10, CO-10 and CO-10 (Bates 0012 - 0015). It was apparently done as part of a CO-10 publication on its personnel and their credentials. The latest work cited was 9/17/XX and the heading was as follows:

DIR-1 (Attorney) CO-10 (City office)
Phone numbers & e-mail of DIR-1

- A faxed CO-10 letter from DIR-3, managing director of CO-10 Corporate & Fiscal Services (Country) to DIR-1 dated 11/21/XX. DIR-3 stated a client wanted them to set up an off the shelf Country agency structure to act and nominee trade for a Country GBC2 entity. Since Country agencies were not a part of their product line, DIR-3 wanted him to see if "we" could incorporate and service such an entity. He then asked DIR-1 if he saw any problems and if not, DIR-1 should find someone in Country acquainted with the agency concept that could provide the essential incorporation and ongoing services.

- An e-mail to ATTN-1, an international tax, trust & estate planning attorney with the CO-14 in Calgary, Country. DIR-1 attaches copies of general information about himself & CO-10, and some CO-10 marketing materials on a hybrid company and offshore non-profits. He also attached a *"marketing type example letter to about 500 of our offshore trust clients after change in '86 and '93"*. He described himself *"As an independent professor and creator/licensor of various tax programs, I spend my time product designing and client closing for a few trust companies, but primarily for CO-10."*

DIR-1 communicates that he is looking to create a hybrid company product for the up to \$ market and was inquiring as to using CO-14 to write and price out a general opinion for Country clients. He said he had a U.S. opinion and would confidentially supply the gist of that opinion so he would *"get exactly what I mean"*. He said CO-10 had experience running 100 hybrids for US "QJ/CFC/PFIC reasons".

He also states in this e-mail that his colleague, RA-7, is well known for inventing offshore insurance tax driven products for the US market (RA-7 of products). *I determined there is a CO-15 in State. RA-7 wrote an article for the British magazine CO-16 in October, 19XX with an update in October, 19XX. The article describes the Product as the creative use of international life insurance utilized to arrange a person's financial affairs so that person will*

never have to pay income taxes again. The article uncovers the unique advantages afforded by employing life insurance in an international estate planning context.

DIR-1 also states that if ATTN-1 had turn key style products for which he could give him his intended client market and produce info sheets with not much work on DIR-1' part, he had "access to pitch and close the clients". DIR-1 also stated that he and RA-7 receive a Country and three US clients a week presently, but turn away or refer two for due diligence reasons. He further disclosed the net worth range of some of the clients he and had worked with over the last three years including 2 billionaires, but he said he wanted to hit the retail market because of the large number of snowbirds in the City area.

4) Information From CO-1 Representatives

DEAN-1, Dean of the CO-1 (CO-1), provided us with an e-mail written by DIR-1 to DEAN-2, CO-1 Dean on 8/1/XX, the date of this e-mail in which DIR-1 answered questions about CO-10's activities on the CO-1 campus.

The second question addressed was if CO-10's presence at CO-1 was only to engage in the activity of finding foreign students for the LL.M. DIR-1 answer was yes and no because CO-10's presence was him. He was not paid, or receiving any benefit in any way, by CO-10 but he was allowed to spend up to % of his time on outside work per the requirements of ABA sanctioned law school programs. He said he had not had time to do so and is cash strung. He said he does not practice law, but does develop tax products through intensive research of tax systems and writes law review articles, which goes hand in hand with his teaching. He licenses these products to CO-10, PWC, or other firms. He stated he could show DEAN-2 examples as long as they were not made public. He does not write legal opinions. He does not publish the materials because they are unique, forward thinking ideas he would prefer to sell, not give away. He would publish after the idea had been sold. He has written three recent articles, one on guarantees, one on Trusts, and one on laws to be introduced next year. He had one in the works on charitable foundations. He stated further on that he does not write legal memorandum because he does not practice law or tax, rather outside law firms do that. If someone calls him and asks about CO-10 he sends them "a form e-mail letter stating due diligence in that he has seen 22 offices and so forth". If CO-10 refers someone to him for a U.S. persons due diligence on it, he provides that on his own accord, using CO-10 stationary and his own account.

He further stated that if CO-10 sent him a wealthy client he would provide due diligence on CO-10. He would also provide information on CO-1. CO-10 has sent him four prospects to date. Three were Country persons and he passed them on to DIR-4, the CO-10 City office contact at the time. He said he never used CO-1's letterhead for any of these matters, either plain paper or CO-10's letterhead.

The third question addressed using CO-1 facilities for business not related to finding students. DIR-1 replied that he was the only person but if DIR-4 (DIR-4, CO-10 Country' office) came by he would not refuse him use of the telephone or a computer within reason and space availability. He said DIR-4's job was to train the LL.M. employees to be efficient and make sure they follow up on CO-10's marketing efforts. He had been on campus three

times since program inception and DIR-1 has requested that he increase his visits to maintain relationships with the Dean's office and suggest things the program needs to do. "He has a very nice floor of an office facility to use on Address with CO-17, so it is a trek out of his way to stop by us." ATTN-2 is shown as a conference speaker in at least the first two Tax Planning Conferences sponsored by the CO-1 and CO-10 in 20XX.

DIR-1 further stated that its (CO-10's) marketing is actually done at its offices like in Country, Country and the Country. The LL.M. program receives calls that CO-10 refers (forwards) and if the call forward is missed, he calls back. He acknowledged getting calls from a variety of persons responding to CO-10's Ecomm advertisements.

The fourth question related to including CO-10's name on the door of the new offices CO-10 funded if DEAN-2 approved the format. DIR-1 responded that DEAN-2 and DIR-4 should speak directly. DIR-1 preferred not to be involved to avoid conflict of interest. He reiterated that CO-10 does not want to conduct business at CO-1 offices other than recruiting students. He said they do not want a U.S. presence, that an "office" would make it taxable in the U.S., CO-10 supports achieving the LL.M. goals because its benefit is in corporate goodwill. It works in CO-1's favor financially, and may for CO-10 depending on student marketing performance.

The rest of the e-mail can be summed up as DIR-1 again complaining about being out of pocket, the problems in trying to be reimbursed, and the potential these conferences could realize in adding students and program success.

5) Information From Others

A third party contact interview was conducted with ED-1, Executive Director of CO-1's Human Rights Program. ED-1 was paid by ORG to develop the on-line LL.M. Program in Human Rights. During this interview, ED-1 recalled DIR-1 had the red and black CO-10 logo on his office door.

A third party contact interview was conducted with AA, former Administrative Assistant to DIR-1 for the LL.M. program in International Tax. AA received payments from ORG as well as from CO-1. AA kept the books for ORG and she wrote out checks for ORG's expenses. AA recalled that when she worked for CO-1 and for DIR-1 she was responsible for answering two phones at her CO-1's office. She was instructed by DIR-1 to answer one phone line as " " and the other phone line she was directed to answer as "CO-10". AA did not know exactly what CO-10 was or what they did, but she did have some brochures on CO-10 for distribution and she knew this was a company in the (Country) and CO-10 had offices in Country. AA recalled that close to the time that she left City (and the employment of CO-1) approximately May or June 20XX, DIR-1 had told her the phone number answered as "CO-10" was the only U.S. contact number.

LL.M. Program – Recruiting Tool for CO-10

In 19XX with the support of the IBFD and the Law faculty at the CO-4, DIR-1 outlined the curriculum for this tax program, produced a draft and the collection process for its materials.

He first taught the tax program in 19XX in Country. He then created the present online version of the Master of Laws (LL.M.) International Taxation & Offshore Financial Centers Program in 19XX with the support of RA-35s CO-11 Academic Publishers and RA-35 and RA-36.

The American Bar Association acquiesced to this program for online delivery in 19XX, the first time offered by an ABA law school and it was initially integrated into the law school program of CO-18. It is not clear when DIR-1 became associated with the CO-10, or what that relationship was in terms of who approached who with the proposal of CO-10 sponsorship for the program. Evidence shows that CO-10 sponsored the program at least from the time it was brought to CO-18 in the United States. DIR-1 resume shows his first presentation on behalf of the CO-10 took place in October, 19XX.

According to its web site, CO-18 was founded in 19XX and was soon recognized as the nation's premier Christian graduate university. Today, CO-18 has grown to encompass campuses in City and City, State, as well as having a strong presence online around the world. Students earn Bachelor's, Master's and Doctoral degrees in the fields of business, communication, divinity, education, government, law, leadership studies, and psychology and counseling. The first three CO-10 Reports, covering the period of 7/XX – 3/XX, advertise the CO-18 internet LL.M. Offshore Tax Planning program and states that more details are available on CO-10's web site website.

The online program admits lawyers, accountants, estate planners, trust officers, and economists from Country, The Country, Country, COUNTRY, Country, and other countries. In 19XX, with DIR-2 of the CO-19 for International Financial Crimes, the program obtained the Anti-Money Laundering and Compliance curriculum.

In 20XX, DIR-1 moved the program to CO-1 (CO-1) CO-1 in City. The reason for this is not known. CO-1 has around law students, and the LL.M. program typically has between and students. In 20XX, DIR-1 hired FAC-1 and FAC-2 (retired IRS attorney) as LL.M. faculty, expanding the U.S. Taxation curriculum, started by FAC-3 in 19XX, into a concentrated curriculum.

In 20XX, a new diploma program began, whereby students could be granted a diploma in just one year instead of taking the two year 28 credit curriculum. In 20XX, DIR-1 was chosen by Central Law & Training, STEP and ITCA to be the sole provider of tax education to the 10,000 plus member practitioner's certifying body. New LL.M. concentrations are being developed in Anti-Money Laundering and Compliance, as well as a curriculum in Trust and Company Compliance.

LL.M./DIR-1 Supporting Entities & Individuals CO-10/CO-10

CO-10 is first listed as a contact office in the U.S. in the first quarter of 20XX, Issue 11 of the CO-10 Report. DEAN-2 as law school dean of CO-1 entered into a marketing contract with CO-10, (having a Country and Country address) effective from 1/1/XX — 1/1/XX. The agreement was signed and returned to CO-1 by CO-10 Trust through CO-10's Country

office. The agreement provided that CO-10, or any subsidiary or entity within the CO-10 organization, would be the sole and exclusive marketing agent for the offshore and international tax courses to students worldwide. CO-10 was paid the commission on all students because supposedly they were all recruited by CO-10. DEAN-1, current Dean of the CO-1 stated that most of the students were from the U.S., with some from Country.

Marketing was to be accomplished by promotional materials CO-10 developed and sent by mail or other means, promotion of the courses at seminars at which CO-10 spoke or was otherwise represented, advertising in local and international publications (including those of CO-10, but only with DIR-1 permission on behalf of CO-1) and through the design and printing of a suitable Course brochure. CO-10 agreed to spend at least \$ per year on marketing. This includes costs of designing and printing brochures and mailing to members of such organizations as CO-20, CO-21, the CO-16, etc.

The agreement describes assistance CO-10 will provide in direct contact with potential students up to the point of securing an application, but receive no funds directly from a student. It also states that CO-10 will not use CO-1 as its U.S. office, including listing CO-1's address or phone number as a means of contacting CO-10, unless approved by the President of CO-1 or the law school Dean. CO-1 is to provide CO-10 with its promotional literature and other logistical support necessary for CO-10 to perform its obligations. It further states that CO-10 shall not act as an agent for CO-1, but DIR-1 will act as liaison between the two, receiving no remuneration from CO-10, and acting in the best interests of CO-1. These liaison duties shall at no time conflict with DIR-1's duties as a law school professor. CO-10 was acting as an independent agent of CO-1.

CO-10 (or an associated company) was to receive a commission determined as a percentage of gross course tuition actually collected from students as following:

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Commissions were payable within 30 days after receipt of course fees from students which were due in four equal payments over a two year period. The agreement is silent with respect to where the money was to be paid. CO-1 goes into the student's background to insure they were qualified to be in the program. Most of the students were not degree seeking and were only interested in areas of concentration.

Dean-1 said that although the wording in CO-10 sites leaves the impression they constructed a building for the law school program (*CO-10 section of the website states "CO-10 sponsors the LL.M through charitable donations which have included funding of the construction of the offices that house the program "*) all they did was spend about \$ to remodel existing offices to accommodate the needs of the LL.M. program.

Dean-1 stated that on November 24, 20XX CO-1 sent a letter to CO-10 in Country & Country that they would not be renewing their contract with CO-10 when it expires on 1/1/XX. He has never had communications with CO-10, all negotiations were held with the previous Dean (DEAN-2). GE-1 (CO-10 CEO) has been on campus several times visiting with DIR-1. Dean-1 stated he suspected DIR-1 and GE-1 were friends socially.

In the 8/1/XX e-mail from DIR-1 to DEAN-2 referenced earlier in this report and pertaining to CO-10 activity on the CO-1 campus, the first question regarded the extent of CO-10's marketing territory. DIR-1 answered that CO-10 was engaged to find all LL.M. students. He explained how CO-10 was assuming all of the costs and risks of marketing the program and CO-1 neither had a marketing budget for the LL.M. or assumed risk. He stated that CO-10 lost money because the commissions do not meet costs, but they could make money in future years if the program did well. CO-10 loaned money to the program the first year because it was "in the hole" and he expected they would do so again if need be. DIR-1 emphasized that money went to the school because he does not need it. It comes from CO-10 because he knows CO-10. He stated that CO-10 gets no advertising from the program and its name is not on CO-1's web site.

DIR-1' comments on CO-10

On February 7, 20XX an investigative interview was held at the City Internal Revenue Service office located at Address, City, State. Present for the interview was DIR-1, RA-3, RA-8, RA-9, RA-10 and IRA. The purpose of the interview was to secure DIR-1' testimony and to discuss available documentation. Part of the testimony secured related to DIR-1' relationship with CO-10 and his activities based on certain documents that indicated in DIR-1' own words that he was developing and licensing tax products. Attached as EXHIBIT B are pages excerpted from the investigative interview. The page numbers referenced in the following paragraphs are the pages from interview as noted in the upper right-hand corner. Testimony secured included:

- DIR-1 stated that he never worked for CO-10 in any capacity (agent, representative, employee, etc.) but that occasionally CO-10 would refer someone to him. DIR-1 has referred clients to him since the time he first started the tax program at CO-18s University (page 86). DIR-1 would advise the client if it was something he could do and the client would pay CO-10. CO-10 would retain % - % of the fee after expenses and the remaining split would come to him (page 95).
- In response to questions about the CO-10 literature that depicts DIR-1 as head of their City office, DIR-1 stated he can't speak for CO-10 but CO-10 did refer people to him. He said they were potential students because CO-10 marketed students for the LL.M. Sometimes they were potential clients of about () in any given year (page 103) resulted in a paid engagement. DIR-1 said he would answer all calls by starting to talk about the tax program. He said some would say well they were calling because they were referred by CO-10 for tax advice (page 105). He said % of those people did not materialize into consulting clients for him because he was not a U.S. tax practitioner, only international (page 105). DIR-1 later in his testimony acknowledged that he didn't think that CO-10 had a separate phone line (number) coming into the LL.M. offices, but maybe they did. He said he didn't think there was a separate phone (page 131).
- For the clients that paid him DIR-1 only gave them advice on what he thought was the best structure and way to go forward, he never actually structured anything (page 113). He said CO-10 referred the client to him expecting to get the structure business after his advice. However, he said that he was very independent. Many times he told the client they

needed to "give everyone a fair shot" if he thought CO-10 might not be the best to handle their situation. He encouraged them to research online and look at all the companies out there and see what works best for them (page 114).

- When DIR-1 was asked about the e-mail he sent out to U.S. clients dated 2/13/XX (EXHIBIT C) regarding CO-10 structures with a CO-10 e-mail address for him, DIR-1 stated that student referrals were coming in from that e-mail and CO-10 set it up for student marketing also because the CO-1 computers and e-mail wasn't functioning very well. DIR-1 said he sent out these information sheets to potential clients who had been referred to him. It was not a mass mailing. He may have sent out 25 – 50 of these a year to those who contacted him and maybe five of those contacts crystallized into advice for which the client paid him through CO-10 (pages 131 – 137). DIR-1 was not paid by CO-10 for marketing their products unless a client received advice from him. When asked if DIR-1 was CO-10's agent in the U.S. he stated he was a referral person, not an agent. He was a referral source (page 147).

- DIR-1 stated he doesn't know the internal workings of CO-10. He knows it is a company but the term CO-10 is just an acronym, a trading name. He said CO-10 (CO-10) was also just a trading name and they were the referring arm of CO-10. He said CO-10 has never had a U.S. physical presence but that "there were lots of other referral people". He knows he wasn't the only one because he received so few calls "and they stopped referring stuff to me" (page 115).

- Regarding the CO-10 address shown in certain materials as Address, City, DIR-1 stated that it was the CO-22. He said "They had other people they refer to". He said he didn't want to say who was on that lease, but it was certainly a referral agent. DIR-1 stated he did not have an office or live there (page 117).

- DIR-1 stated DIR-4 at CO-10 Country referred RA-11 to him. RA-11 needed U.S. advice and he didn't know how to do these tax eliminations. DIR-1 knew from conferences these things were possible and so he suggested maybe three firms RA-11 should consult, one in State and CO-23 (CO-23) for sure. DIR-1 had met RA-12 at conferences, but they were a firm he had no previous or subsequent affiliations with. DIR-1 did not know what the transaction was that CO-23 marketed to RA-11. He does not understand how these financial transactions work (pages 195 – 196). DIR-1 received no fee on this transaction because RA-11 was not his client. However, DIR-1 did what he could do for RA-11 and set him up with a foreign bank account with CO-24 (this is a Country asset and wealth management private bank). DIR-1 stated he told RA-11 that he must report the account as a U.S. person, couldn't have a secret credit card account, and would need a tax opinion if he was going to do this kind of thing (page 121). DIR-1 stated he has not worked with RA-12 on a tax product because he doesn't do what RA-12 does. He is a company guy, he knows companies (page 202).

- DIR-1 stated that RA-11 contacted him like two years ago and was asking for estate planning advice or something. RA-11 mentioned that his attorneys were going to sue and referred to the transaction set up by CO-23 as a Son of Boss transaction. RA-11 told DIR-1 it was water under the bridge and he had come clean (page 194 – 195). DIR-1 said he never received any fees for that transaction from anyone, just for setting up the CO-24.

- With respect to the M/M transaction donors to ORG, DIR-1 stated of the 100 or so names on the donor list he may have actually spoken to one or two on the phone for assurance that ORG was a tax exempt charity. He said these donors were referred by CO-25, CO-26, CO-27, CO-28 and one or two others, but not CO-10. DIR-1 said he would have met

RA-13 at a conference and asked for ORG to be put on their approved list of donation possibilities because ORG raised money for the LL.M. program (page 97). He said RA-13 told him that they managed assets for wealthy individuals and at the end of the year they advise their clients to donate to charities and DIR-1 wanted ORG on those charity lists (page 99).

- DIR-1 stated when asked if any CO-10 affiliate have any transactions or dealings with CO-23 that he was neither of those parties so it was better to ask them. He couldn't be certain and he didn't want to speculate. He said that he did not bring RA-12 to CO-1 (CO-1) because he did not have the authority to hire people. RA-12 was already "relationshiping" with CO-1 and when RA-12 came to CO-1 he was one of the people RA-12 "relationshipped" with. He implied that RA-12 was brought on to teach U.S. tax courses in the regular law program and DIR-1 "suggested it would be a good thing" if "he could also teach in the LL.M. program" (page 123).
- DIR-1 stated that CO-10 would furnish the LL.M. program with CO-10 Reports and DIR-1 would send them out with school brochures as a goodwill gesture for CO-10's help in marketing for students. He said CO-10 paid \$ - \$ per year in marketing costs for the LL.M. program. Then when asked if he did any marketing for CO-10 he said "*I would try to solicit clients for myself*" but wasn't very successful at it. People would call up and he would send them materials about CO-10 and explain that if they needed consultation on international issues he could help but they would have to go to CO-10 for actual structuring (pages 129 - 130).
- With respect to EXHIBIT D, the e-mail to ATTN-1 an attorney in Country about DIR-1' marketing activities with RA-7, he said it was all just marketing hype. DIR-1 said he talked to lots of Country law firms about trying to create some kind of company that would work in Country, but it just never happened. He couldn't do it. There's nothing he knows that works in Country. He said the gist of the Product (RA-7 also taught at CO-1) was a life insurance policy that's earnings were tax deferred and you could borrow against the policy tax free. He says the references to his developing products and marketing for CO-10 is also hype. DIR-1 said he tried. and tried to develop a product for U.S. and Country clients but has never been successful at designing an international tax product that worked . Nor was he able to "*manage to ferment and crystallize a product that I could sell to the US. market*" (pages 158-161).
- In response to the portion of DEAN-2's e-mail from DIR-1 (EXHIBIT E) where he stated that DIR-4 had a very nice floor at the CO-17 in which to work was that he did not know the relationship between ATTN-2 and CO-10. He assumes that CO-10 is sending ATTN-2 referral clients. Beyond himself CO-10 has lots of client referral people. He was just one of them (page 172).
- Regarding DIR-1' resume (EXHIBIT F) describing various worldwide works DIR-1 had done for CO-10 he again stated that he tried to do these things but failed, it didn't work. He was not an employee of CO-10 in Country, he was on his own, having been referred by CO-10. For each of the specific projects he had listed he stated that for one reason or another they were unsuccessful and in most cases he never received any money. DIR-1 said "*I'm just trying to make myself look big so that people would hire me*" (page 180). He didn't have a big firm behind him, so he didn't get the work.
- DIR-1 was asked how CO-10 marketed its products/obtained its clients. DIR-1 stated through the internet. He said DIR-4 was a "*relationship manager*". He marketed in Country

but "he'd fly over to shake hands with me" (page 182). When asked about other referral people, DIR-1 stated ATTN-3 who has a law firm in State and someone in a law firm in City. DIR-1 stated that he was the only contact shown in CO-10's materials in the U.S. because he would filter out potential students of which he probably obtained 100 over the years this way (page 185). DIR-1 stated he didn't know but it was possible that some of the LL.M. students became referral agents or marketers for CO-10. He never actively marketed any company in the LL.M. program. He was neutral and taught all companies all things. CO-10 had other students in the LL.M. program like RA-5. He said most of his students were 40 — 50 year old professionals who already had a tax degree and a practice, so for the most part they were not looking for jobs. He said if students came through CO-10 because of CO-10's advertising and then they set up a relationship with CO-10 or something, they may have told him in passing, but generally he would not know about it. If CO-10 had an opening he would post it like he would for any other CO-10 competitor company. He said it was possible that CO-10 worked with some of the students who went through the program, but a lot of them already worked for competitors of CO-10 (page 186 — 192).

- Regarding the Assignment of Options to ORG DIR-1 stated he did not prepare the document, he assumed that RA-14 or RA-15 did, and does not know what this stuff means. He didn't care what it was called people were giving to ORG only what the exact cash amount was ORG would get. This was what he put on the donee acknowledgement letters. He didn't want the risk of holding an asset represented as being worth so much but when converted to cash was much less. He is not a finance guy who understands options. He said the options were sold and the cash transferred by wire into ORG (pages 213 — 220). DIR-1 said his intention was to follow up on the donors and raise more money but he had a problem because RA-14 wouldn't send any more donors in 20XX when they discovered ORG didn't have an IRS determination letter yet. He said it was because the Service is so slow (page 221).

- DIR-1 said that the Board of ORG (DIR-2 & himself) voted to sell any asset donated to them. When asked why they didn't take just cash he responded that they did. He said options were the same as real cash but they took the options because these high net worth individuals have "pregnant stock or accelerated real estate ". The asset gets donated. It's just what normally happens (page 223). DIR-1 stated he told RA-16 up front that he was not going to play the valuation game and he wanted him to understand that "we want to receive cash in the bank". He told RA-16 "sell this as soon as possible. I want cash in the bank And if I don 't have it, no letter. Because I don 't know its value. I can 't give you a value." RA-14 sold the options, DIR-1 stated did not even know what selling it meant. He would wait for the counterparty to sell the options and wire the proceeds to ORG (page 225). Towards the end, in answer to RA-3 question of whether ORG or the donor sold the assigned options for cash he said "RA-14, the donor. I always thought it was the donor." DIR-1 also answered that the acknowledgement letter gave the amount of the cash received from the sales proceeds.

Operations of ORG

As stated in the application for exemption, ORG was established to "operate exclusively for educational and charitable purposes. In particular, the Foundation will provide CO-1 ("CO-1 ") LL.M programs in Tax and Human Rights with contributions in order that the programs will be able to provide support to their students. The Foundation is viewed as an integral fundraising activity required by the LL.M. programs in order to continue their success. "

*"The Foundation will hold conferences, meetings, and assemblies to provide a forum for the discussion and dissemination of relevant information and data to promote a better understanding of international, economic, tax and fiscal topics. The Foundation will sponsor at least three conferences each year at CO-1 featuring such economic and fiscal topics."
"The Foundation will edit and publish papers, magazines, pamphlets, periodicals and books."*

A third party contact letter was sent to CO-1 on July 22, 20XX for information with respect to ORG. A response was received on July 2, 20XX (EXHIBIT G). Questions asked and responses provided are shown below:

1. Was CO-1 aware that ORG was established to be an organization set up to support the CO-1? If so, were there any agreements between ORG and CO-1 concerning the funding of these programs during 20XX through 20XX? If so, please provide a copy of the agreement.

"CO-1 was unaware that ORG was established to be an organization set up to support the CO-1."

2. If possible, please explain how ORG's fundraising was "an integral fundraising activity" required for these programs to succeed.

"ORG fundraising was not an integral fundraising activity required by the LL.M programs or any other program at the CO-1."

3. The information in the application indicates that multiple conferences involving economic and fiscal topics were held at CO-1. It is our understanding that these conferences were not actually held at CO-1, but CO-1 was a sponsor and/or involved with these conferences sometime during the period 20XX through 20XX. Please provide a statement to explain the relationship between CO-1 and ORG as it pertains to these conferences. If a contract exists, please provide a copy of the contract.

"There was no relationship between CO-1 and ORG with regards to the above conferences nor is there a contract".

4. If the LL.M. programs did not receive funding from outside source, such as ORG, would the programs have been terminated?

"The operation of the LL.M programs was in no way dependent upon funding from ORG or any other particular outside funding source."

CONFERENCES ORG provided material for four conferences for the audit as follows:

- 1st Annual Congress – May 2nd through May 4th 20XX – Country, Country
- 2nd Annual Conference – December 4th through 6th 20XX – City, State
- 3rd Annual Congress – June 4th through 6th 20XX – Country
- 4th Annual Conference – March 25th and 26th 20XX – City, State

Review of the ORG's records for tax year 20XX indicated no financial support to the two conferences held in 20XX. The following was noted in the review of the conference materials provided:

- ORG was not listed as a conference sponsor for any of the conferences.
- There was no reference to ORG anywhere in the conference materials.
- DIR-1 and DIR-2 were listed as either participants and/or presenters at the conferences.
- No information was provided on conferences subsequent to the last conference mentioned above.
- For all of the above conferences, CO-29 (CO-29) was shown to be sponsor.

Information provided for the audit indicated a possible relationship between CO-29, DIR-1 and DIR-2 so internet research was conducted to gather additional information. These conferences were listed on CO-29 website and the available information indicates CO-29 is the premier professional cross-disciplinary society that educates, trains and certifies professionals in international tax, compliance, anti-money laundering and corporate and computer security.

CO-29's website stated:

"The Society hosts two three-day conferences annually that provide a forum for government officials, expert practitioners, and academics to present papers and talks on selected topics, as well as spend quality social time together at the Society dinner, lunches, and cocktails."

Per the bylaws of CO-29, DIR-1, DIR-2 and RA-17⁴ are all founding members of CO-29. See EXHIBIT H for additional information on CO-29.

The 20XX Form 990 does report an educational conference. It does however report a net loss from Special Events of \$. The actual figures will be discussed later in this report in the Income category.

RETURN INFORMATION - INCOME reported on Form 990 is as follows:

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*Power of Attorney (POA) POA stated in a response dated October 22, 20XX, "ORG has submitted its amended Form 990 for 20XX and the IRS should have a copy." This return was not filed with the revenue agent even though there was an on-going examination. This return has not posted to Internal Revenue Service's (IRS's) internal system.⁶ The 20XX income will be addressed separately in this report based on a review of the summonsed bank records.

20XX Income

The banking information from CO-30 (Account #number) was summoned since ORG stated the bank records were destroyed. Review of the bank information revealed that the income reported on Line 1 a the 20XX Form 990, \$, agreed with the amount deposited into the

account. See attached EXHIBIT I for specific amounts and source of deposits.

From the beginning of the examination, DIR-1 stated the amount reported as income was from charitable donations and were the results of fundraising. Per response dated 02/21/20XX received from POA, it was stated:

⁴ FAC-2 will be discussed later in this report.

⁵ The original Form 990 filed on October 17, 20XX was filed with Block K checked stating that ORG's "gross receipts are normally not more than \$". The 20XX Form 990's Balance Sheet was left blank

⁶ Document was not summonsed since the Service policy precludes issuing a summons for a document that is in our possession.

"DIR-1 did not directly contact any of the donors prior to their contributions to ORG. However, DIR-1 did personally contact asset managers who represented wealthy individuals as a means of soliciting charitable contributions for ORG. Typically, many asset management firms would attend the international tax conferences that DIR-1 would attend on behalf of ORG and/or the LLM program of CO-1, which ORG supported. These assets management firms would have booths at the conference, where they would promote their services. DIR-1 would approach an asset management company, tell them about ORG and its charitable mission, and ask the asset management company to refer any of its wealthy clients who were interested in making a charitable contribution to an educational or tax organizations to ORG. It is a common fundraising technique for charities to approach private bankers or asset managers when the charity is soliciting charitable contributions. Moreover, it is common for asset management firms to direct wealthy clients to charitable organizations, with which managers have some knowledge or relationship. Had DIR-1 NOT approached the asset management teams and/or private bankers, ORG most likely would not have received all of the contributions that it did in 20XX. However, DIR-1 did not contact any donor directly (other than RA-17) in 20XX. More importantly, DIR-1 did not specifically solicit contributions of foreign currency options from the asset managers. Rather, he asked the asset managers to direct donors to send cash to ORG, but was happy for whatever contributions ORG could receive. DIR-1 personally contacted the asset managers and private bankers, but it was the asset managers and private bankers who would identify potential donors and refer them to ORG."

Income was received in the form of Assignment Agreements. The assignment agreement income was reported on Line 1 a — Direct Public Support from Contributions, Gifts, Grants, and similar amounts received. Provided for the audit was a listing of Assignment Agreements that were for individuals and companies that donated Put/Call Options to ORG. ORG issued an acknowledgement letter to each of the contributors stating the options were received as a "charitable gift". There were a total of contracts listed on the Assignment Agreements involving individuals from various locations throughout the as well as some contracts with individuals in the

The acknowledgment letter issued to the contributors included the following statement:

"The ORG recognizes your charitable gift, dated (date, of (amount). Due to present economic conditions and recession and economic fluctuations in the economy resulting there from, as well as the potential for economic fluctuation because of military conflict and terrorist actions, the Foundation's Board of Directors voted to sell your gift in order to generate cash assets. The proceeds from the sale of your charitable gift property that has been added to our endowment."

The total donated per the Assignment Agreement listing provided by ORG was \$. This is approximately % of the total gross contributions received by ORG in 20XX. However, a reconciliation of the bank statements showed the full total of \$ was from the assignment agreements. Although the Assignment Agreements indicated that ORG received puts/calls, the banking records summoned indicated that ORG received cash via wire transfers from various trading companies. Per review of the bank deposits in 20XX, there was also Assignment Agreement income of \$ in 20XX. EXHIBIT I

The Service has determined that these amounts were from tax shelter transactions reported on Notice 20XX-81. The Service has disallowed the contribution amounts on the Form 1040 of all participants (contributors) in the sheltered transactions.

20XX Income

The bank accounts reflected more deposited into the CO-30 account in 20XX than was reported on the Form 990. The amount which should have been reflected on the Form 990 was \$ as shown in EXHIBIT I. Reported on Page 1, Line L Gross Receipts was \$ while reported on Line 1 a was contributions in the amount of \$. The discrepancy was determined to be \$ from the bank deposits to the amount reported on Page 1, Line L and a discrepancy of \$ from the bank deposits to the amount reported on Line 1a.

The income received/reported in 20XX in the amount of \$ was reported on Line 1 a — was from CO- and two separate deposits as follows:

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Information presented for the audit indicated that RA-17 is the Executive Director of the Tax Clinic and Visiting Professor of Law at CO-1. RA-17's biography from CO-1's website states:

"ATTN-4 was an attorney with the Internal Revenue Service for 37 years before moving into private practice in 20XX. While serving at the IRS, RA-17 worked in the following capacities: Estate Tax Attorney (19XX-19XX), Estate Tax Attorney Manager (19XX-19XX), Appeals Officer (19XX-19XX), Appeals Manager (19XX-19XX, 19XX-20XX), and Tax Shelter Program Coordinator at the National Office (19XX-19XX). At CO-1, RA-17 serves as the Executive Director of the Tax Clinic and an Adjunct Professor of Law in the Graduate Tax Program (LL.M), and he teaches Civil Tax Procedure."

During the meeting held with DIR-1 on May 9, 20XX, DIR-1 acknowledged that RA-17 is a colleague and co-worker.

The Form 990 for tax year ending December, 31, 20XX reported an educational conference as a special event as follows:

Gross Receipt from Conferences	\$	
less: Contributions Included on Line 1a		-\$
	\$	Line 9a
less: Direct Expenses	-\$	Line 9b

Net Loss from Special Event

-\$

Line 9c

RETURN INFORMATION - EXPENSES Expenses reported on Form 990s are as follows:

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*Power of Attorney (POA) POA stated in a response dated October 22, 20XX, "ORG has submitted its amended Form 990 for 20XX and the IRS should have a copy." ORG was requested, on more than one occasion, to provide a copy for the on-going examination, but failed to comply.⁸ The 20XX expenses will be addressed separately in this report based on a review of the summonsed bank records.

Program service expenses are those incurred to carry out the organization's mission. In an interview with DIR-1, DIR-1 stated the purpose of ORG is to provide charitable assistance to LL.M. in International Taxation and Offshore Financial Centers and the LL.M. in International Rights programs at CO-1. DIR-1 also stated that they support programs in the field including international policy/fiscal policy and one of the goals of ORG was to bring knowledge back from other countries to the United States.

DIR-1 area of specialty is International Tax Policy/Fiscal Policy. In his position as professor at CO-1, DIR-1 has met people through CO-50 (CO-50) which is, per DIR-1, the largest educator in the Country. ORG was formed in 20XX, but DIR-1 stated he was already an expert in his field and was already published. DIR-1 stated he spends about 40 to 60 hours a month handling ORG matters and has done so for years while at the same time being a full-time professor for CO-1.

20XX Expenses — All

The \$ expense reported as Program Service on Form 990 for 20XX was for the development of a computer program for CO-1's LL.M. in Human Rights. A third party interview with the recipient of the payment, ED-1, was held on May 10, 20XX. Present were Revenue Agent IRA and Manager M-IRA. ED-1 demonstrated the on-line program that she developed for CO-1's LL.M. Program in Human Rights. She verified the receipt of \$ from ORG via wire transfers was for the development of this program. Per ED-1, this was a one-time payment for her to research existing programs; locate and/or develop materials for the site; and market the on-line program. ED-1 stated while serving as the Director of Recruitment of the LL.M. Program in Human Rights she Ibid-5

⁸ A review of current internal IRS documents reflects the amended return was processed in late February 20XX. As of the date of this report, the revenue agent has not received the copy from the processing center. was approached by DIR-1 in about April 20XX to put this program together. No grant request was submitted to ORG. ED-1 did not receive a Form 1099 or W-2 from ORG

Management/General Expenses in 20XX comprised of \$ of legal fees and \$ of bank fees. The expenses in 20XX were limited and, from review of the bank records, it was determined the management expense was two wire transfer payments of \$ each to the law firm CO-32. The

bank statement reflected one of the payments was reversed on 09/27/20XX with the comment "Book credit for ORG...Rev of our dbt to yr acct 09/20/XX..." ORG incorrectly claimed \$ more in legal expense in 20XX than actually paid.

20XX Expenses — Program Services

Program Service reported on Form 990 for 20XX included \$ in grants/allocations; educational research of \$; and other miscellaneous expenses of \$. Grants/allocations were paid to CO-33, \$, and CO-1, \$.

CO-33 is a 501(c)(3) exempt organization that is run by DIR-5. DIR-5 is the mother of DIR-1. ORG's Form 990 reflected Donee's Relationship as "None". In an interview with DIR-5 as the Compliance Officer of ORG, DIR-5 stated that the payment was for educational purposes. DIR-5 also stated "that no one in my family received any of the \$". Subsequent to the meeting, a written recap of the meeting was provided to DIR-5 for review and comment. POA provided a document entitled "Information for RA-18"⁹. The document was presented by POA as the response from DIR-5 and this document indicated changes to statement as follows:

"I did say the \$ was used for educational purposes. I should not have said this. I should have referred the answer to my CPA. "

"Query: What is the time limit for the use of this money? "

"The funds were placed in the operating account of CO-33. From the operating account money was spent on education: specifically (but not all inclusive) rides 2 & 3 times a day (7 days a week) to 12 step meetings, purchases of educational material for tenants and employees, costs of attending educational conferences for employees and tenants, materials for college, GED and literacy classes, services of tutors, physicians, nurses, a psychologist, drug counselors, social workers and others involved in the education of CO-33 tenants."

"Since the \$ was placed in the operating account one could argue that family received some of the money because family members were employees of CO-33. Most salaries were paid by grants deposited into the employee account. One grant paid approximately seventy percent of four salaries so approximately thirty percent of those salaries were paid by the operating account. "

Although a signature was requested from DIR-5, the document provided by POA was unsigned.

⁹ RA-18 was an attorney retained by DIR-1 to assist in responding to the Internal Revenue Service in this matter.

The \$ donation to CO-33 was further scrutinized when during the formal interview held with DIR-1 on February 7, 20XX, information was obtained that DIR-1's Form 1040 for 20XX was amended to include \$ from CO-33. The payment to CO-33 from ORG and the payment from CO-33 to DIR-1 were in the same year (20XX). When directly questioned if the \$ donation was the payment given to him, DIR-1 stated these were "different

transactions ".

A review of the bank account information reflected checks totaling \$ were paid to CO-1 in 20XX. This included some checks with the annotation of a loan for RA-19 and a check earmarked for a specific person (RA-10). Although it appears these checks were designated for a specific person, these expenses will be allowed without further development since they were paid directly to CO-1.

The total was determined as follows:

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A third party request to CO-1 resulted in the presentation of Check # for \$ dated 07/01/20XX payable to "CO-1" from CO-29. This check was signed by DIR-1. EXHIBIT J is the acknowledgement from CO-1 (as provided by ORG) and a copy of the \$ received by CO-1 as provided by the University. This payment was not made by ORG and therefore cannot be shown on the Form 990 as Program Service expense of the organization.

POA submitted a response on August 1, 20XX in regards to ORG's relations with CO-1. POA's response discusses the letter from A-Dean, Assistant Dean for Development, CO-1 dated July 21, 20XX which states "As you requested, here is a list of the gifts to CO-1 that are credited to ORG.... " One of the donations included the \$ check to CO-1 mentioned above.

POA explains this payment as follows: "...ORG has indirectly supported CO-1 by its payment to the CO-29 of \$. The purpose of this payment was to fund a conference that was held by CO-29 in conjunction with CO-1. DIR-1 and DIR-2 recall that it was the Third Annual Congress (held June 4-6, 20XX/Country). DIR-2 recalls that the conference materials prominently displayed CO-1's name and is in the process of locating these materials. DIR-1 recalls that CO-1 and CO-29 executed an agreement for CO-29 to administer the conference on behalf of CO-1." POA's response later states, "If ORG had made this \$ payment direct to CO-1, it is unlikely that the IRS would question ORG's support. Although hindsight suggests that ORG should have made the \$ payment directly, the result at the end of the day is the same. ORG provided financial support to a conference sponsored and affiliated with CO-1."

Reported as "Educational Research" was \$. Based on review of the checks and third party contacts, the expenses were reallocated into the following categories based on the Country of funds:

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See EXHIBIT K for individuals paid and relevant amounts.

The payment categorized as "Exempt Purpose" was Check # , dated 08/04/XX, and included the annotation "Research Grant". This was paid to RA-20 for researching and writing an article published in CCH and Tax Note International. A letter from RA-20 and a copy of the article he prepared that was presented for the audit. The article was copyrighted

to RA-20. ORG does not have a specific grant criteria application or approval process as confirmed by interviews and discussions with DIR-2 and DIR-1.

Payments categorized as "Loans" were checks that included the annotation of a loan in the memo line of the check. There were no loans reflected on ORG's balance sheet. For the individuals identified in this category, there were no loan documents presented in response to the Information Document Request (IDR) #22. There were no loan repayments in tax year ending December 31, 20XX from these individuals.

Payments categorized as "Payment for Services – CO-1 Employees" included payments to CO-1 employees who were working in the LL.M. program in International Tax. DIR-1 was the Director of this program. In some cases, these expenses were expenses that were not allowed or would not be paid by CO-1. For example, student workers were not allowed to work beyond a specific number of hours. However, DIR-1 paid these individuals to work beyond the allowable number of hours and therefore, he paid these individuals and classified it on the checks as "research grant", "bonus", "severance pay", etc.

Payments categorized as "Payment for Services – DIR-1" include payments to individuals who provided services that benefit, directly or indirectly, DIR-1 as the Director of the LL.M. Program in International Taxation, at CO-1. These expenses may have been indirect expenses of CO-1; however, these were payments that were not allowed per the University's own policy. Internet research was conducted to locate third party contacts and some of these individuals were contacted to determine the purpose of their payments as follows:

RA-21 – Posted on ORG's most recent website, under "Some of the Foundation's Charitable Accomplishment", was information that RA-21 is a financial journalist who is working on an encyclopedia in the field of International Tax and Company Compliance for CO-34. Provided for the audit was a couple of e-mail messages from ATTN-5 of CO-34 to DIR-1 from December 20XX which states the following:

"RA-21 has so far spent two weeks on the project and expects to be able to work full tim [sic] on it from now. That essentially means your arrangement with him would start December 1st", subject to any separate agreements with regards to the two weeks worked over the last couple of months."

"I understand your concern regarding the returns on the projects covering the editorial investment you have committed. The following points may be helpful in further considering this issue:

- *This is a long term project which will be built up over a number of years and the returns will therefore build over time as well. It would be difficult for us to guarantee that royalties will cover the entire editorial fees, which is in any event unlikely for the first year or first couple of years, depending on how quickly we can build content and market share. The intention is clearly that over a period of years things would even out in cumulative terms."*
- *I would be perfectly happy to increase the royalty rate once a certain number of subscriptions have been sold. This should speed up the process outlined above.*
- *A special offer to the Society of Fellows¹ could help build market share more quickly*

than would otherwise be the case.

We are determined to aggressively market and sell this new service worldwide based on the USPs you have identified in the proposal document. "

The e-mail messages do not mention ORG. Internet research was conducted in an attempt to make contact with either RA-21 and/or CO-34 for possible contact as a third party was unsuccessful. CO-34, as well as RA-21, are located in the Country and it was not possible to locate a personal address for RA-21. The available address for CO-34 was not a valid address and further research reflected CO-35 acquired CO-34 in August 20XX per a press release. The press release included the comment "*CO-34 is a specialist legal publisher with particular strengths in titles on European Law and Financial Services Law and Regulations for lawyers and professional advisors.*" Contact was not made to CO-35 for information relating to CO-34.

Various documents posted on the internet reviewed during the audit process include background on DIR-1. Part of the posted background includes the notation that DIR-1 was listed as a "consultant editor" for CO-34. The information provided on RA-21 and CO-34 do not support that the work done by RA-21 is related to ORG.

ATTN-3 – ATTN-3 submitted a statement to POA RA-4 addressing the \$ payment received by him from ORG. Per the statement "*... on or about July 28, 20XX, I received a check in the amount of \$ from the ORG to write articles to be published and used by the RA-35 H. & RA-35/RA-36 Graduate International Tax Program, CO-1. Attached are my two papers regarding money laundering and the COUNTRY Patriot Act... which were submitted to CO-50 to be published.*" Third party contact to CO-50 requesting verification of the articles resulted in the response of "*We have no knowledge of this person.*" (EXHIBIT L)

RA-22 – RA-22 stated that she was paid for editing and typesetting a potential law review article. "*DIR-1 requested that I be his editor for this work These services were performed for DIR-1.*" RA-22 was paid \$ an hour for editorial work. ORG did not receive editorial credit for this article.

¹⁰ Society of Fellows was the former name of CO-29.

RA-23 – RA-23 was a student at CO-1. Review of the checks indicated he was paid for services rendered for the LL.M. Program in International Taxation. DIR-1 directed the activities for the work that was performed. RA-23 submitted a statement to POA which stated "*I served as a student employee to DIR-1, as well as to other professors in the Tax Department, and was paid by CO-1 as a research assistant. While employed by CO-1 CO-1 as a student employee I undertook research for the article*

I did this research under the specific direction of DIR-1, reporting back to him regularly with my research. DIR-1 credited me in his article as his CO-1 research assistant." As shown in EXHIBIT M, the article mentioned above was published in the Business and Tax Law Journal in 20XX. The article reflected the author was DIR-1 and included comments from DIR-1 as follows: "*I express*

much appreciation to my wife, Wife, for her utmost patience; to my research assistant RA-23 and to the CO-1 Law staff who assisted with long nights of microfilm and microfiche research, and to RA-24 for the constant brainstorm sessions." There was no mention of the funding/support received from ORG nor was ORG given credit or acknowledged by DIR-1.

RA-25 – RA-25 received \$ as an advance for future work. This indicates that this payment for future services to be rendered.

RA-26 – RA-26 stated *"During the time I worked for DIR-1 I considered myself employed by him. All my work was given directly by DIR-1, sent to him and reviewed by him. I never spoke to anyone at the ORG, nor received any work from anyone at that foundation."* RA-26's statement also stated *"In both 20XX and 20XX I would review the Tompson chapter in Saunders and Dean 's publication International Tax Systems and Planning Techniques. As part of the reviews I would update or write sections into the chapters to reflect changes in US tax law which had occurred over the past year, I would incorporate in any new sections which were to be included by other tax professionals and proofread and bluebooked all citations."* A recent posting to the CO-1 (City, State) website included information on DIR-1¹¹ which included information that DIR-1 "is the author for the US Chapters for International Tax Systems and Planning Techniques, a series by Roy Saunders and Miles Dean published in loose-leaf and on Checkpoint." There was no mention of ORG or RA-26's involvement. See EXHIBIT N for information posted on CO-1's website.

POA provided information concerning RA-26's payment as follows: *"We understand that the \$ grant to RA-26 in 20XX was for research work she performed for ORG throughout the year. The research that RA-26 provided while serving as research assistant for ORG was related to ORG 's exempt purpose of supporting and promoting the International LL.M program at CO-1. For example, RA-26 provided significant research on international tax systems and planning techniques. "*

RA-24 – An appointment was scheduled with RA-27 to discuss the purpose of the payments he received. When scheduling the aforementioned appointment, a brief discussion was held with RA-27 regarding the payments he received from ORG. RA-27 stated he had researched and written some lengthy documents and he was "just told" that he should have reported something like \$ for the payments he received. Some of the payments were for rental vehicles and RA-27 stated he had car problems and needed a car. Since he was having car problems, DIR-1 paid for his rental car. RA-27 indicated he knew DIR-1 from CO-18 CO-1 in City. RA-27 failed to appear for the scheduled appointment. When he did not appear, a follow-up phone call was made and RA-27 informed Revenue Agent IRA that he would not be meeting and any further questions should be directed to his attorney.

¹¹ Per the "Program Handbook 20XX-20XX" posted on CO-1 website, DIR-1 is listed as the Assistant Dean and is responsible for "Academic Issues".

A review of the submitted documents included statements/invoices submitted from RA-27 that showed research was conducted "for DIR-1".

POA provided a statement concerning RA-27's involvement with ORG. RA-27 was a

research assistant for ORG from March 20XX until December 20XX. POA's stated *"Initially DIR-1 recalls RA-27 conducted ORG's research while working as a legal researcher at CO-18 CO-1 in City. RA-27's research for ORG related to money laundering, economic terrorism, and prosecuting - all topics relating to ORG's charitable mission. RA-27 would travel to State to conduct further research at CO-1' law library and present his findings to DIR-1 and DIR-2, so ORG could incorporate his work into either the conferences that it was sponsoring or the publications it was drafting."* The response went on to state that ORG compensated RA-27 by paying for his research time and reimbursed his rental car expenses. *"ORG does not recall reimbursing RA-27 for his lodging during this time period."* POA statement included the comment *"Although some of RA-27's invoices may state that research was done for DIR-1' the actual research was for publications and/or conferences sponsored by ORG."*

A review of ORG's financial records reflected ORG paid Check # for \$ on 12/20/20XX to CO-1. Third party contact to CO-1 resulted in confirmation that this payment was for Fall 20XX Room and Board for RA-27 which was paid by ORG.

RA-28 – RA-28 received payments for vacation and severance pay. This indicates these payments were for services rendered.

In summary, the payments to the above individuals appear to be payment for services rendered rather than actual "educational research" as noted on the Form 990 or as "research grants" as noted on the checks. By categorizing these expenses incorrectly, ORG has failed to properly report compensation for services rendered as either W-2 wages or Form 1099 non-employee compensation. In addition, indirect benefits were provided to DIR-1 by making the LL.M. Program appear to be more success by having lower costs reported to the University than the true cost of the program. In some cases editorial credit was claimed by or given to DIR-1 rather than ORG. The research and information provided during the examination was unable to verify that ORG had editorial credit for any published materials.

Received as the result of a third party contact with CO-1 was a document entitled "Memorandum of Understanding" which stated the following:

"To the extent that DIR-1 personally assimilates costs associated with the International Tax LL.M program in the 20XX-01 academic year, he will inform the Law School of such costs on a regular basis. In the 20XX-02 academic year, he will be paid these costs if the program generates net revenues in excess of \$ that year. If net revenue from the program in the 20XX-02 academic year are insufficient to allow recovery of DIR-1 costs from the 20XX-01 academic year, than a payment will be provided in the 20XX-03 academic year if the program generates net revenue in excess of \$ that year. If net revenue from the program in the 20XX-03 academic year are insufficient to allow recovery of DIR-1' cost from the 20XX-01 academic year, then payment will be provided in the 20XX-04 academic year if the program is expected to generate net revenue in excess of \$ that year. "

This document was executed by DIR-1 as Director, International Tax LL.M. program and by DEAN-2, Dean CO-1.

During the formal interview held with DIR-1 on February 7, 20XX, one of the documents discussed during this interview was a letter address from DIR-1 to RA-29 dated October 14, 20XX. Excerpted from this letter, EXHIBIT 0 Page 2, was the following: *"As long as my program is profitable, I will continue to be employed by the University as the administrative and academic director of my program, either as a tenure track professor of law or, failing a tenure vote, as a member of the law faculty through five-year rolling contracts. Alternatively, failing a tenure vote, we may agree to move my program and myself as director to sit under the graduate school, reporting directly to the President. Alternately, the University may request that I laterally move my program to another University, for which I have two contemplated offers.... "*

"As I do now, I will control my future budgeting based upon my present fiscal budget and my present expenditures will be based on my future budgets, subject to a minimum \$ projects being built into the budget."

20XX Expenses – Management/General

Management/General Expenses reported on Form 990 for 20XX worthy of discussion includes \$ in legal fees. Of this amount, \$ was paid to RA-2.

RA-2 is the brother-in-law to President/Co-Director DIR-1. RA-2's wife, RA-30, is DIR-1's sister. RA-2 was elected as secretary of ORG and served from the approximately the end of December 20XX through the end of 20XX per RA-2's oral testimony. Information secured from the State's Secretary of State reflected RA-2 was appointed ORG's registered agent on April 7, 20XX.

During the examination, we initially identified two payments to RA-2 from ORG's account with CO-30, Account #number. The payments were made to "RA-31, LLC". This included:

Check # dated 09/30/20XX for \$ Check # dated 11/20/20XX for \$
IDR # was issued on March 16, 20XX requesting information on payments to RA-2. This request included "a statement to address any other payments made to family members of any of ORG's Officers or Board of Director members for services rendered for the period 20XX through the present."

To verify the purpose of these payments, ORG provided correspondence and invoices received from RA-2 for his legal services which included:

- 1) A letter and an invoice dated September 17, 20XX was provided for the payment of \$ for legal services relating to The Foundation for Fiscal Studies that was completed on behalf of ORG.
- 2) A Retainer Agreement dated November 20, 20XX for the \$ payment. Per this agreement, *"in return for professional services rendered and to be rendered the ORG agrees to pay a retainer of \$ for professional services to be rendered by RA-31, and RA-31, LLC for a term of 36 months commencing on January 1, 20XX."* The Retainer Agreement goes on to state that RA-2 would deduct \$ per month for administrative services and would deduct at a

rate of \$ per hour for legal and consulting services rendered during the agreement period and if "the retainer is exhausted prior to the expiration of the agreement, ORG agrees to pay additional funds" to RA-2 "in increments of \$."

3) Monthly statements billing ORG for services.

Although the \$ expense was paid in 20XX, per the contract, no services were required until 20XX. The statements for April 20XX and June 20XX through March 20XX (date of submission) only reflected \$ per month for "Administrative Services". The other statements reflected deductions for "legal services" as follows:

- January 20XX — \$ — Researching public v. private foundation (5 hours); contributions rules (2 hours)
- February 20XX — \$ — Unable to read handwritten note which includes something about "filings" (1 hour)
- March 20XX — \$ — Telephone call with WB requirements for exemptions (1 hour); public support issue (2 hours); unable to make out third comment (3 hours).
- May 20XX — \$ — Telephone call with WB requirements for BOFD/Meeting Requirements (1 hour)

On May 2, 20XX, a face-to-face interview was held with RA-2 to determine his role in ORG and to acquire additional information concerning payments made to RA-2. Present for this meeting was POA, Form 990 preparer/former POA; DIR-5, former Compliance Officer of ORG; RA-2, former Secretary of ORG; M-IRA, Manager and IRA, Revenue Agent.

During this meeting, RA-2 stated his involvement in ORG included handling the paperwork and other information for ORG that were sent to the Address, City, State address. Specifically, RA-2 stated that letters and bank statements were sent to Address and he would put the information/statements in a folder and this was mailed to DIR-1 in City, State to review. RA-2's understood that DIR-1 would get the necessary paperwork to the accountant, POA in City, State, a suburb of City, State.

NOTE —

April 20XX. RA-2's monthly billing statements indicated ORG was charged during this period for the monthly administrative services.

In the meeting described above, RA-2 stated the income had not been reported on his individual tax returns. A summary of the meeting was provided to RA-2 asking him to review the summary and to provide corrections/additions as warranted. RA-2 responded by submitting a signed written statement with the following comment:

"I did not report the income in 20XX. I intended to report the income in 20XX/20XX/20XX in equal installments. I have been informed that I should have reported all of the income in 20XX. I am amending my 20XX return to reflect this income."

Subsequent to the meeting held with RA-2, financial records for ORG's bank accounts for

20XX were summonsed, received and reviewed. From the summonsed records, it was determined that RA-2 received another substantial payment. This was Check # dated 01/06/20XX for \$.

IDR # 31 was issued on December 8, 20XX to ORG requesting information on the second payment to RA-2 since the January 20XX monthly billing statements from RA-2 reflected a beginning balance of \$ rather than the \$ which was paid as evidenced by the cancelled checks. At the time this payment was made to RA-2, he was officially the secretary of ORG.

A response was submitted on behalf of ORG from Power of Attorney POA (POA) on February 21, 20XX. Per this response, the payment was a *"retainer for RA-2 's professional services to establish the Foundation for Fiscal Studies ('FFS') as a supporting organization to ORG. FFS was established in 20XX, but never obtained exempt status. Thus ORG stopped researching whether FFS could obtain public charity status as a supporting organization. The \$ fee was determined based on RA-2 's hourly rate and the amount of work needed to identify the pros and cons of FFS changing from a private foundation to a public charity and to pursue a private letter ruling from the IRS indicating FFS was a supporting organization."* The response went on to state that RA-2 would *"promptly return any portion for the 1/6/04 \$ payment that exceeds his services to ORG "*.

A subsequent response from POA received 08/01/20XX included a copy of a check from RA-2 and RA-30 paid to ORG in the amount of \$ for repayment of the unused retainer. Also included in this response was a copy of the Form 1040X signed on July 17, 20XX which has been verified as filed with the Service.

The Service has no record of Foundation for Fiscal Studies submitting a Form 1023, Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code. A review of The Foundation Center's website revealed a Form 990 for the tax year ending December 31, 20XX that was filed for Foundation for Fiscal Studies on November 18, 20XX. (EXHIBIT P) ORG is not identified anywhere on the return. No subsequent returns were ever filed for FFS.

12 The Foundation Center is one the most authoritative source of information on private philanthropy in the United States. Part of their service includes making available the Form 990s and Form 990-PFs filed by tax-exempt organization on their website.

20XX Expenses – Fundraising

During the examination, fundraising reported on the Form 990 was identified as one payment, check # dated 11/20/20XX for \$, to RA-30 from ORG's account with CO-30 Account #number.

Provided for the audit was a copy of a "Contract for Services Agreement" dated November 20, 20XX which stated: *"It is agreed that ORG will employ RA-30 for fund-raising, administrative and consulting services. Compensation will be paid up-front in the amount of \$. The term of employment will be for 36 months commencing on January 1, 20XX."*

A third party contact was made with RA-30. A response included a signed statement dated

August 9, 20XX with the following comments: *"I organized files, prepared a database for conferences, prepared materials and brochures for conferences, and supervised the website. The payment was for a 3 year contract for 20XX through 20XX. No W-2 was issued. I intended to report the income in increments in 20XX through 20XX. However, I have been advised that this is not correct. I am amending my 20XX return."*

No fundraising materials were submitted to reflect the fundraising activities that were undertaken 20XX through 20XX. The summonsed bank records reflected only one contributor, FAC-2, in 20XX and no deposits from contributions, gifts or grants in 20XX or 20XX.

In reviewing ORG's application for exemption, ORG was questioned concerning the use of professional fundraisers. Per the response submitted to the Service from POA Bruce Hopkins on February 3, 20XX, *"You inquired as to the use of professional fundraisers. That is not contemplated. The present plan is to have one or more employees of the Foundation solicit contributions and grants."* This response included a declaration signed under *"penalties of perjury"* by DIR-1, President of ORG. Although professional fundraisers were not used, in lieu of using employees of the foundation DIR-1 used his sister, RA-30, who received a three year contract with full up-front payment, that included fundraising as one of the activities to be accomplished as part of the agreement.

20XX Expenses – Investments

The last expense to be addressed in 20XX is investments in the amount of \$. During the examination, ORG provided information on its various investments. EXHIBIT Q is a recap of the investments for 20XX and 20XX. As reflected in the exhibit, investments included highly speculative investments in stocks including stocks privately held and stocks that traded over-the-counter (OTC). These investments ultimately resulted in overall loss to ORG.

POA provided the following statements with her February 21, 20XX response:

"ORG used reasonable business judgment and care when it selected the investments.... Its board of directors examined current market conditions to identify investments that would generate a positive return for the charity, while also being an investment that had some relationship to ORG's charitable mission of supporting CO-1's international LL.M program. That is why several of the investments were for international companies. For example, ORG purchased shares in CO-36 in Country because the CO-36 is located in City, a Country community that has skyrocketing real estate values. ORG's directors believed when they acquired the shares in CO-36 (and its underlying real estate) that its value would continue to grow."

Some of the investments ORG were involved in and the end results include:

- As shown in EXHIBIT Q, CO-36 referenced by POA was purchased by six different payments totaling \$. This investment was sold in late 20XX per a letter from RA-32. RA-32's letter stated that he is *"the majority owner, of the CO-36, a hotel and real estate venture, CO-37 and CO-25 "*. RA-32's letter goes on to state that the *"CO-36 investment*

was intended to be a five year investment for development and improvements of the property and renovations to the hotel. ORG requested to sell out of its investment at an early stage in October. I have purchased its interest in December 20XX. "

POA provided with her response dated August 1, 20XX verification that the CO-36 was sold by ORG for \$ and this amount was deposited into ORG's bank account. Based on the financial records reviewed and documents provided, the overall loss to ORG for this one investment was \$ (purchase price of \$ less sales amount \$).

- As shown in EXHIBIT Q, ORG purchased \$ of CO-38 in two transactions (paid on 10/15/20XX and 12/19/20XX). This investment was sold in late 20XX for \$ per information provided in POA's response dated August 1, 20XX. Based on the financial records reviewed and documents provided, the overall loss to ORG for this one investment was \$ (purchase price of \$ less sales amount \$).

- ORG purchased _____ was purchased in October 20XX for \$ and sold for \$ on April 13, 20XX per POA's response to IDR #26 received February 21, 20XX. This security was purchased in the name of DIR-1 and sold as an investment of DIR-1 by CO-39 rather than as an investment of ORG. ORG claims the share certificates were erroneously issued in the name of DIR-1 and some e-mail messages indicating the shares should be registered in the name of ORG. When the stock was sold. the shares were still in the name of DIR-1.

- CO-40's website state "CO-40 is one of the largest privately owned and operated CO-41 located in the State of State." The headquarters for CO-40 is located at Address, City, State. This is the same address CO-1 had its off-campus location for the LL.M. Program in International Tax which was the program run by DIR-1. CO-40 is a privately traded company and we have no information on the current status of ownership of CP Motion.

BANK INFORMATION FROM SUMMONSED RECORDS 20XX

Income

Income from 20XX was determined based on deposits from summonsed bank records. Although POA has told us that the Form 990 for the year ending December 31, 20XX has been amended and filed, the return has not posted to the IRS internal system. In POA's response dated October 22, 20XX, POA declined to provide a copy to the revenue agent stating "ORG has submitted its amended Form 990 for 20XX and the IRS should have a copy."

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There were no contributions, gifts, grants or similar amounts deposited in 20XX. Income from Special Events is the result of ORG paying for materials to be reproduced for the LL.M. Program in Human Rights. The materials used in the LL.M. Program in Human Rights were turned over to a copying service, CO-42, and the bills from CO-42 were paid by ORG upon completion of the service. The reproduced material was subsequently sold to the students in the Human Rights program at or close to cost. The payments from the students were paid by personal checks and the amounts received from the students were deposited

into ORG's account. This was not intended to be a money making activity.

The Internet Business Law Service (IBLS) revenue was four payments of \$ each paid to ORG for preparing and publishing international tax books used by students in the LL.M. program. IBLS is the internet platform hosting the course materials and providing IT support for the students and staff. A third party contact was made to IBLS to clarify and confirm the information provided. Testimony was received from RA-33 who stated that IBLS received payment from CO-1 for putting the materials on the internet platform. IBLS subsequently made payments to ORG since IBLS was paying for the publishing rights for this material. When verifying the purpose of the payments, RA-33 of IBLS stated, "*DIR-1 directed that payments be made to ORG as it was the producer of the tax books being used during the course of study.*"

Third party contact was made to CO-1 concerning the payments made to IBLS in 20XX and 20XX. Per the response received from RA-34, Associate Dean of Academic Affairs, which stated "*The total amount paid to IBLS in 20XX and 20XX was \$. No payments to our knowledge were returned or refunded from IBLS.*"

Various internet sites were reviewed to learn more about the Law (LL.M.) program¹³. DIR-1 was listed as the founder of the CO-43 (a.k.a. CO-43). The LL.M. Program in International Tax was started at CO-18 CO-1, City, State in 19XX. The LL.M. program was operated in conjunction with CO-1, City, State from 20XX through 20XX. The LL.M. program is currently offered by CO-1, City, State. DIR-1 has been involved in the program since its inception in 19XX and is still currently involved. DIR-1 was employed by all three universities during the time the programs were operated at those universities.

As stated previously, the LL.M. program was established and operating in 19XX before ORG was incorporated on February 13, 20XX or recognized as a tax-exempt organization on May 10, 20XX.

Secured from CO-1 was a list of the courses offered in the LL.M. program and the description of the courses. This is attached as EXHIBIT R. In comparing the courses offered for the LL.M. program at CO-1 to the individuals paid for specific work, it was observed that none of the individuals paid worked on developing any of the LL.M. program courses.

From information publicly available via the internet reviewed as part of the audit process, it was determined the original materials used in the LL.M. program were developed and published by RA-35 and RA-36. A third party contact letter was sent to RA-35 & RA-36 to request information on the LL.M. program. When asked what the CO-43 is, RA-35 stated that the program started "*at CO-18 as an international tax program to educate foreign students who did not have the means in their countries to go to college.*" The response went on to confirm that the "*program was moved from CO-18 to CO-1*" and is now offered by CO-44 "*using RA-35 & RA-36 books published by five law publishers whose professors have approval to use as source materials.*"

When inquiring what the RA-35/RA-36s' relationship/affiliation was with each of the universities mentioned above, RA-35 stated "*The only relationship is free use of our name*

that is known for 60 years in international trade and taxation through distribution of our books by the legal publishers."

When inquiring what the RA-35/RA-36s' knowledge, relationship and affiliation with ORG and its directors, RA-35 stated that he had no knowledge/relationship of ORG and had "never heard of it"; for DIR-1, RA-35 provided information that "DIR-1 is the Director of the RA-35/RA-36 International Tax Program at CO-44 and our understanding is he is an Assistant Dean in charge of the RA-35/RA-36 Internation [sic] Tax Proram [ski"; for DIR-2, RA-35 stated "DIR-2 is co-author with RA-35 & RA-36 for the book updated three times a year titled 'International Trust Laws and Analysis' published by CO-11 Legal International in the Country. "

Questions were asked about the materials used in CO-1's LL.M. Program. Per RA-35, "our books published by five legal firms were and are used as source materials in classes and approved by the published to be used.... The five publishers pay me royalties for books sold...all publishers have copyrighted [sic] RA-35/RA-36 books under their names... the copyrights are owned by publishers, CO-45 (CO-45), CO-11, CO-35, CO-46, CO-47 formerly now by CO-35. "

¹³ Including CO-1; CO-1; CO-48; CO-43; and CO-49

The complete response provided by RA-35 is at EXHIBIT S.

20XX Expenses - Totals

A review of the summonsed bank records revealed disbursements totaling approximately \$. In the absence of a Form 990, the Service attempted to allocate the expenses into appropriate categories based on review of the checks, third party contacts, and a summary spreadsheet provided by ORG.

EXHIBIT T is the summary spreadsheet ORG provided for 20XX. In comparing the bank account information with the amounts reflected on the summary sheet provided, it was determined that the summary did not include all the expenses/withdrawals from the account.

EXHIBIT U shows the expenses allocated to most of the categories shown above and will be discussed further. Not reflected in this chart are \$ expenses relating to ORG paying for materials to be reproduced for the LL.M. Program in Human Rights. This was discussed previously in the report under Special Events (Line 9a) and resulted in a net loss of \$.

20XX Expenses – Exempt Purpose

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Payments categorized as "Exempt Purpose" included a couple of minor payments and a \$ payment to CO-50, Country. The information on ORG's summary spreadsheet indicated the \$ payment was for "Diploma agreement/publishing book on tax compliance". Third party contact made to CO-50 confirmed that there was a contract between ORG and CO-50 to work together to provide course material for distribution under the Advanced Professional Development (APD) series. As part of the agreement, ORG transferred \$ US to

CO-50 as a contribution towards the initial set up of the program. CO-50's response also stated *"we confirm that DIR-1 is acknowledged as the author of the Advance Professional Development Course entitled "International Taxation – Principles and Structures."*

20XX Expenses – Loans

Payments categorized as "Loans" were checks that included the annotation of a loan in the memo line of the check or reflected the expense as a loan on ORG's summary spreadsheet. There were no loan repayments in tax year ending December 31, 20XX from these individuals per review of the bank records. There were no loan documents provided for the examination.

20XX Expenses – Payment for Services – CO-1 Employees

Payments categorized as "Payment for Services – CO-1 Employees" included payments to CO-1 employees who were working in the LL.M. program in International Tax. Some of the payments included the annotation "fall bonus" on the check. DIR-1 was the Director of this program. In some cases, these expenses were expenses that were not allowed or would not be paid by CO-1. For example, student workers were not allowed to work beyond a specific number of hours. However, DIR-1 paid these individuals to work beyond the allowable number of hours and therefore, he paid these individuals and classified it on the checks as "research grant", "bonus", "severance pay", etc. Other expenses in the category included \$ payments to three individuals – RA-37, DIR-2, and RA-38 – for "teaching" per ORG's summary spreadsheet.

Also included in this category of expenses were payments totaling \$ to CO-1 that were ORG claimed was "donations" to the CO-1. This included the following:

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20XX Expenses – Payment for Services – DIR-1

Payments categorized as "Payment for Services – DIR-1" include payments to individuals who provided services that benefit, directly or indirectly, DIR-1 as the Director of the LL.M. Program in International Taxation at CO-1. These expenses may have been indirect expenses of CO-1; however, these were payments that were not allowed per the University's own policy. Some of the individuals who received payment in tax year ending December 31, 20XX were the same individuals as mentioned previously in the tax year ending December 31, 20XX information. This includes payments to RA-21, RA-25, and RA-26. These individuals and the services they performed was previously discussed under the 20XX development. The other individuals paid were students at CO-1 and, per the summary spreadsheet they were paid a "fall bonus". Since these individuals are not employees of CO-1, the services performed for the bonus is attributed to DIR-1.

20XX Expenses — Reimbursements

Payments categorized as "Reimbursements" were payments identified on the checks as reimbursements and were paid to two individuals. Check #\$, dated 08/24/XX, for \$ to RA-39

for " " and Check # , dated 11/30/XX, for \$ to DIR-2 for "Reimb for CO-51."

20XX Expenses — Donations

Payments categorized as "Donations" included payments totaling of \$ to CO-1 that the university identified and acknowledged as gifts to CO-1.

20XX Expenses — General and Management

Payments categorized as "General and Management" were primarily for payments for accountant/attorney fees \$ directors' liability insurance \$; the second payment of \$ to RA-2 paid on 01/06/20XX which was discussed under Management/General Expenses for 20XX; and a payment to DIR-5 for rent of Address, City, State.

On January 5, 20XX, a check was written to DIR-5 in the amount of \$. This represents a three year up-front contract for rent. The rent is for the office space for ORG located at Address, City, State. The space has been described as the room above the garage. DIR-5 resides at Address.

IDR #32 was issued to obtain additional information on the rent payment. Per the written statement provided by POA on 02/21/20XX *"ORG and DIR-5' did enter into a Commercial Lease with ORG on November 1, 20XX. The term of the lease is 36 months. ORG most likely lost its executed copy of the lease due to . The monthly rent was \$".* The property leased by ORG *"stores its files, conference materials, research records, and various publications.... Although ORG conducts its charitable activities around the globe and conducts most of its research activities in State, it is less expensive for ORG to store its records in State than in State. DIR-1 usually ships ORG's records to State via third class mail after ORG completes its research projects, conferences or publications. Moreover, ORG must have a registered office in State because it is a State nonprofit corporation."* The property *"serves as ORG 's registered office. Other activities conducted at this address include organizing ORG 's research materials and donor records. The landlord also provided a computer, printer and telephone access to ORG".*

The financial records reviewed did not reveal any payments for postage for the shipment of *"records to State via third class mail"* from State or from any other location. ORG was requested to provide verification that an office was maintained in City and specifically requested to provide verification of the shipping of documents. None has been provided. The conferences that are referenced in POA's response have been determined to not be an activity of ORG. There were no donors to ORG in 20XX. It has not been established why ORG would need an office to organize the research materials and donor records when the individuals compensated for research were located in various locations and the financial records reflect only one donor, FAC-2, in the years under examination and RA-17 donated before the office was established.

According the State Secretary of State Corporation Database, on the report filed January 31,

20XX:

Domicile address: Address City, State Mailing address: c/o POA,
Address, City State DIR-1 address: Address, City State

The report filed on April 7, 20XX with the State Secretary of State shows the following:

Domicile address: Address, City, State
Mailing address: c/o POA, Address, City, State DIR-1 address: Address,
City, State

20XX Expenses — Benefit to DIR-1 (inurement)

Payments categorized as "Benefit to DIR-1" include \$ of payments from ORG to DIR-1 and \$ of payments to an CO-52 credit card, Account #number, which was DIR-1' personal CO-52 card.

Most of the payments directly to DIR-1' were transferred directly from ORG's CO-30 account into DIR-1' account with CO-30 (Account #number). One payment made on July 16, 20XX was a check, # , issued directly to DIR-1. Dates and amounts of payments/transfers to DIR-1 are shown below:

TABLE DELETED

IDR #34 was issued on December 8, 20XX to request information on payments to DIR-1. This IDR requested information on the \$ payment issued to DIR-1 via Check # on 10/06/20XX as well as for information on the payments detailed above. For the payment issued in 20XX, the IDR requested a statement to address specific services rendered for this payment and information on the filing (or lack of filing) Form W-2/Form 1099 for this payment.

On February 21, 20XX, POA's submitted a response which included the comment "*ORG's \$ payment to DIR-1...was erroneously marked 'Services' by ORG's accountant. DIR-1 believes that \$ actually was an advance for several conferences that DIR-1 attended in the Fall of 20XX. DIR-1 would promote the LL.M program during these conferences.*" This statement contradicts available information for the following reasons:

- Although POA's letter states the payment was erroneously classified as "services" by ORG's accountant (POA), Check # dated 10/06/XX included the annotation "Services to CO-1". RA-4 did not write out the checks and therefore did not make the annotation concerning the payment was for services.
- DIR-1 reported the income on his personal Form 1040 for tax year ending December 31, 20XX per POA's statement "*DIR-1 paid tax on that amount and has provided his Form 1040 for 20XX to the IRS in the audit of his personal taxes.*"
- On May 11, 20XX DIR-2, co-director of ORG, was interviewed in person and he stated the \$ was payment for DIR-1' services to ORG;
- At the conclusion of the meeting held with DIR-2 on May 11, 20XX, DIR-2 provided a

written letter, addressed to POA dated 04/03/20XX, that stated *"We voted to compensate DIR-1 as a \$ services contract for the year 20XX for his long hours of work with establishing the Foundation documentation and administration."*

- DIR-1 did not raise this as an issue in this examination until the investigative interview held on February 7, 20XX which was after IDR # was issued requesting a statement to address specific services rendered and an explanation about the lack of a Form 1099 or W-2.

POA's response goes on to state that the funds transferred into DIR-1' account were for advances for various conferences and *"in accordance with ORG 's reimbursement policy...DIR-1 would reimburse ORG for such advances within 3 — 6 months of his receipt. DIR-1 repaid ORG \$ on August 20, 20XX. DIR-1 was reimbursing ORG for its earlier advances to him."* POA's response went on to state DIR-1 also repaid the following amounts:

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In reviewing the information secured via the summonsed bank records, Check # for \$ from DIR-1' CO-30 Account #number was deposit on 08/20/20XX. There was no deposit into ORG's account for \$ during November or December 20XX per review of the bank records. Records for tax year ending December 31, 20XX were not requested or reviewed since it is outside the 20XX through 20XX years under audit.

For one reimbursement, \$ on 02/23/20XX, POA provided a partial copy of DIR-1' bank statement for February 20XX. The statement was for CO-30 Account #number-9 in the name of DIR-1 and was for the period February 18, 20XX — March 17, 20XX. Most information on this statement, including summary of activities, balances, other transactions were removed (sanitized), and the one amount left disclosed was for Check # for \$. This statement did not provide verification of who the check was actually issued to and is not considered verification of repayment of funds to ORG.

For the other payments listed above, ORG did not provide verification of these amounts being repaid by DIR-1 and is, therefore, not considered to be reimbursement of the funds paid to DIR-1. POA did include information in her February 21, 20XX response which stated *"ORG has requested its bank statements for 20XX from CO-30"*, but no additional verification of the repayment has been provided for the audit.

POA's response goes on to state *"ORG made these expense advances to DIR-1 so he could travel to conferences on ORG's behalf. The amounts in Tab 16 [relating to the advances questioned in IDR #34] relate to the personal component of DIR-1 travel and were ultimately repaid by DIR-1. The amounts for which there are reimbursement sheets relate to the business expenses that directly connected with ORG 's exempt purpose. As a practical matter, ORG should have offset the expense reimbursement with the expense advance that it had previously paid DIR-1. However, ORG did not do this. Instead, ORG sought repayment from DIR-1 for the expense advance amount plus 15% interest"*.

No information, other than POA's statement, has been provided to confirm DIR-1 repaid the amounts paid to him. Also, nothing has been provided to show the repayments, if made,

included interest. Under IRC §3121(d), officers of an organization are considered to be employees. Payments issued under a non-accountable plan should be included in an individual's income and later, if the expense is ordinary and necessary business expense under IRC § 162 and if the elements of IRC §274(d) are met, the expense deduction can be claimed by the individual. Since the claimed repayments occurred outside the audit years, no information has been requested or provided concerning how DIR-1 handled this issue.

The payments to CO-52, Account #number, were as follows:

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IDR #25 was issued on April 4, 20XX to obtain information on the payments made by ORG to DIR-1's personal CO-52 credit card. The last two payments above, Checks # and # , were not part of IDR # since complete financial information was not available until the bank records were received via summons.

IDR # requested verification of the expenses including verification required under IRC §274(d); requested verification of the business purposes of the expenses under IRC § 162; and requested how the expenses were determined to be an expense of ORG rather than a personal expense of DIR-1. This IDR also requested that ORG provide a statement from CO-1 if the reimbursed expenses relate to the University.

In response to IDR # , POA provided a statement and some documents. The submitted statement was not signed, but included the following comments:

"One of ORG's purposes is to provide support for the LL.M in International Taxation. Support may be expressed in a variety of ways. The Board of ORG represented by DIR-2 and DIR-1 decided ORG would partly expend its funds in the manner of these reimbursements. "

"The LL.M is unique in that it is an online distance learning program. Most students do not live within a 100 mile radius. Thus, an opportunity for students for face-to-face meet, network, and undertake discussions with the program director is through meals, a customary approach in all cultures. Other LL.M international taxation programs undertake social events..., as well as this being a customary practice of law schools and universities in general.... "

"Further, the program director does not have significant involvement with the JD students because of the LL.M. program duties. Thus, orientation and graduation represents an opportune time to network with the JD students and to create goodwill for the LL.M program amongst that student body."

The information presented included information on various social activities including a flyer for a cocktail reception for the IFA Congress (September 20XX); packet of information for an event called "Global Tax Symposium 20XX" which appeared to be an event sponsored by CO-1; e-mails from a RA-40 (with a CO-1 e-mail address) inviting CO-1 administrators, faculty, staff to an event called "Law Alumni Network Happy Hour" in City in April 20XX and City in May 20XX.

The response continued with the comment: *"Separately, ORG has other charitable purposes than the LL.M program in International Taxation. By example, promoting education in the field of international taxation through conferences and publishing, which the board has sought to promote. Such activities require networking and development over an extended time frame. Networking and development requires meeting different individuals, sometimes many times, over time, to develop a relationship to achieve some purpose."*

Provided for the audit was the excerpts from the CO-52 statements and the Reimbursement Forms submitted to ORG from traveler DIR-1. In reviewing the documentation, the following was noted from the reviews:

1) Reimbursement Form filed by DIR-1 for the period 03/10/20XX through 03/25/20XX totaled \$.00. The form indicated this was for the "ASOF Conference, speaker meeting, copy costs, and Human Rights program". Attached to this form was a copy of the ORG's \$ check, # , paid to CO-52; CO-29's 4th Annual Conference cover page reflecting conference dates of March 25 & 26, 20XX; information on the 5th Annual Offshore Financial Services Summit held the 26th and 27th of May 20XX in Country; and some excerpted pages from DIR-1's CO-52 statements. Most of the expenses listed on the reimbursement form were for meals. For the meal expense, a persons name and/or company name was listed on either the CO-52 statement, but no actual receipts were provided nor was the specific business purpose noted for these meals. One expense on 03/24/20XX for \$ was for "conference photocopies & materials". The conference was an activity of CO-29 and not of ORG.

2) Reimbursement Form filed by DIR-1 for the period 03/27/20XX through 04/25/20XX totaled \$. This was reimbursed by ORG's Check # on 05/10/20XX. The form indicated "Witwatersrand University Masters Program also left over CO-29 conference receipts/City, Country". Verification provided included CO-52 statements with some annotations indicating expense was for ORG; airline receipt from City to Country, Country; and taxi receipts. One expense on the CO-52 statement was for CO-53, City, Country for \$ on 04/25/20XX. No actual lodging receipt was provided. Sufficient information was not provided to verify expenses listed were for ORG's exempt purpose nor was information provided to establish the expenses as an ordinary and necessary business expense of ORG's.

3) Reimbursement Form filed by DIR-1 for the period 05/18/20XX for Adobe Acrobat purchased by CO-52 and reimbursed by ORG by Check # , in the amount of \$, paid to CO-52. The invoice for this purchase indicates it was shipped to DIR-1 at CO-1's CO-1's address. This amount is de minimus and could be an ordinary and necessary expense of ORG. It is therefore allowed without further verification of the expenses.

4) Reimbursement Form filed by DIR-1 for the period 04/25/20XX through 05/19/20XX totaled \$. This was reimbursed by ORG's Check # on 05/20/20XX. The form indicated the expenses were for LL.M. Graduation Dinner and for what appeared to be some individual names. Attached to this reimbursement form were excerpts from the CO-52 statements with ORG noted on it for dining and bar expenses. No actual receipts provided; no verification of ORG's business purpose for these expense and IRC §274(d) pertaining to recordkeeping not

met.

5) Reimbursement Form filed by DIR-1 for the period 06/05/20XX through 05/22/20XX totaled \$. This was reimbursed by ORG's Check # on 07/16/20XX. The form indicated the expenses were for IBFD (International Bureau of Fiscal Documentation). Provided for verification was excerpts of CO-52 statements. The expenses listed included restaurants discussed below; \$\$ for "CO-54, City, Country" on 06/05/0XX; gift item at City Intl Airport for \$\$; and \$\$ for "CO-55". Internet research was conducted for IBFD and it was determined this company is based in The Country and per, their website site, "Since 19XX, tax practitioners from all over the world rely on International Bureau of Fiscal Documentation (IBFD) for authoritative expertise on cross-border taxation. IBFD is the portal to high quality independent tax research, international tax information and education with the aim to enable customers to do their work more quickly and efficiently." CO-55 was researched and it was determined about the time of the \$\$ charge, this non-profit organization held the City Celebrity Domino Night. No specific information on what was received for the \$\$ payment.

For the meal expenses, it was determined from the information submitted by ORG and by the reimbursement vouchers provided by CO-1 that the charges reflected on the CO-52 statement was equally split between CO-1 and ORG. No information was provided as to why it was split and the specific business purpose of the expenses. The expenses included the following:

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6) Reimbursement Form filed by ORG for the period 06/30/20XX through 07/11/20XX totaled \$. This was reimbursed by ORG's Check # on 08/27/20XX. The form indicated the expense was for a dinner with CO-56 and for an unidentified expense at a City restaurant. No actual receipts provided; no business purpose established; and recordkeeping requirements of IRC §274(d) not met for these expenses.

7) Reimbursement Form filed by DIR-1 for the period 08/09/20XX through 11/29/20XX totaled \$. The form indicated the expenses were for IBLS, Student Orientation, LL.M. and RA-21. These expenses include lodging expenses of \$ on 09/28/20XX at the CO-27, City, State and \$\$ on 08/09/XX at CO-58, City, Country. The other expenses were for items such as \$\$ for "hosting the incoming orientation for JD students"; meal with RA-21 in Country on 09/26/20XX for \$\$; "LL.M. orientation" meal in City for \$\$ and parking at City International Airport from 11/23 — 11/29/20XX for \$

As a recap, IBLS is the internet platform hosting the course materials and providing IT support for the students and staff. IBLS received \$ from CO-1 for this service and IBLS subsequently paid ORG \$ which was paid at the direction of DIR-1. RA-21 was previously discussed and available information did not support a business relationship between RA-21 and ORG.

In reviewing the payments to CO-52 (see previous table), there was no payment corresponding to this reimbursement form. There was a payment of \$ made to CO-52 by Check # on 09/01/20XX and these expenses may be part of that reimbursement, but the

dates do not agree and the amount paid to CO-52 is substantially more than the listed expenses.

8) Reimbursement Form filed by DIR-1 for the period 08/11/20XX through 08/21/20XX totaled \$ and was for "Student Orientation". For verification, ORG provided excerpts from the CO-52 statements and some receipts. Some of the receipts were just the charge slips, but three were legible and included details. Some of the details noted included the following – \$\$ for cheese, fruit and shrimp cocktail on 08/13/20XX; \$\$ for a bottle of champagne (Perrier Jouet Rose Fleur De Champagne) on 08/15/20XX at Co-60 in City, State; and \$\$ for a bottle of Grey Goose, J & B, LR Brut, and five single Red Bulls on 08/14/20XX at the Co-59 in City, State for a party of 6 guests. None of these receipts specified who was entertained or the specific business purpose of the expense. These expenses are not ordinary and necessary under IRC § 162 and even if they were determined to be ordinary and necessary, these expenses relate to student orientation of the LLM program and would be expenses of CO-1.

In reviewing the payments to CO-52 (see previous table), there was no payment corresponding to this reimbursement form. There was a payment of \$ made to CO-52 by Check # on 09/01/20XX and these expenses may be part of that reimbursement, but the dates do not agree and the amount paid to CO-52 is substantially more than the listed expenses.

9) Reimbursement Form filed by DIR-1 for the period 09/05/20XX through 09/23/20XX totaled \$. This was reimbursed by ORG's Check # on 10/01/20XX. One of the expenses on this reimbursement form included an expense of \$\$ on 09/05/20XX which was designated on the reimbursement form as "lodging expenses". The actual receipt provided with that dollar amount included the preprinted name of "CO-61" in Country and there was a line for gratuity. This is not verification of a lodging expense. The other expenses were for meals and did not meet the recordkeeping requirements of IRC §274(d).

10) Reimbursement Form filed by DIR-1 for the period 10/02/20XX through 10/04/20XX totaled \$\$ but was reimbursed as \$ per annotation on the voucher. The comments on the reimbursement form stating the nature of the request was not clear. Attached to this voucher was information on the International Fiscal Association (IFA) Congress 20XX in Vienna. Third party contact to CO-1 on travel vouchers filed by DIR-1 during this period of time resulted in information provided that the IFA conference was related to DIR-1' position as an employee of CO-1 and the conference expenses were, therefore, paid for by CO-1. The conference was from 09/05/20XX through 09/10/20XX. These expenses on this reimbursement form do not appear directly related to the conference since CO-1 paid for the expenses relating to the conference. The reimbursement form included \$\$ for a rental vehicle and \$\$ for lodging at CO-58, City, Country. Business purposes of these expenses were not clear.

In reviewing the payments to CO-52 (see previous table), there was no payment corresponding to this reimbursement form. This reimbursement form was approved by DIR-2 on 10/23/20XX and it is possible the \$ payment transferred from ORG's account with CO-30 to DIR-1's account with CO-30 (#number) on 11/04/20XX may be for this reimbursement.

11) No verification or documentation was provided for the final three payments to CO-52 reflected in the chart above. It was noted that these payments were made on the same date, 10/01/20XX, and were paid by three consecutive checks (# , # , and #). The total for these checks were \$\$.

Summary of CO-52 Payments:

In reviewing the documents submitted by ORG, the only expenses which appear to be allowable as related to ORG's exempt purposes include the purchase of Adobe Acrobat on 05/20/20XX for \$ and IBFD purchase on 06/05/XX for \$\$. This was a total of \$ \$ for business. The other payments made by ORG to CO-52 were determined to be either personal expenses of DIR-1, payments of another organization's such as CO-29 or CO-1; or unsubstantiated as an ordinary necessary business expense of ORG.

In comparing the total payments made by ORG in 20XX to CO-52, \$, to the amount determined to be for ORG's exempt purpose, \$\$, less than 2% of the payments were verified to be for ORG's business purpose.

CO-1 was contacted as a third party contact to obtain information concerning the university's policy concerning the expectation that DIR-1 entertain and pay for meals, without reimbursement, for other professors or students during orientation, during the school year or at graduation.

Per the written statement from CO-1 dated November 10, 20XX — "Based on University policy, it would not be expected for a faculty member to entertain and pay for meals, without reimbursement, for other professors or students during orientation, during the school year, or at graduation." (EXHIBIT V)

CO-1's response referenced above and subsequent response provided on July 2, 20XX (EXHIBIT G) were shared with ORG and POA submitted a response on 08/01/20XX to address CO-1's letters to us. For the first letter dated November 10, 20XX, POA's response stated: *"DIR-1 would take students, other professors and visiting faculty out to dinner. This promotes ORG's charitable purpose because it rewards students for work that they did for ORG and promotes ORG's charitable activities by providing details about ORG in general and CO-1's LL.M program in particular and by encouraging students, visiting faculty and other professors to inform others about the LL.M. program. DIR-1 was either reimbursed by ORG or CO-1 for these expenses. DIR-1 recalls that he never was reimbursed twice for the same expense. If CO-1 did not reimburse DIR-1, the ORG would, which is consistent with its exempt purposes, including supporting and promoting CO-1's LL.M program.*

For the second letter dated July 2, 20XX, POA's response stated: *"...CO-1 distances itself from ORG and states that it 'was unaware that ORG was established to be an organization set up to support the CO-1.' Further, CO-1 states that ORG was not an integral fundraising activity for CO-1 nor were the operations of the LL.M. program dependent on funding from ORG or any other particular source of outside funding. "*

"ORG respectfully disagrees with CO-1's characterization of its relationship with ORG.

First, CO-1 was aware and even acknowledged the financial support that ORG provided it. For example, in a July 21, 20XX letter, CO-1 thanked ORG for its 'support over the last several years' and identified four direct gifts from FEA¹⁴. CO-1 also indicates that ORG has indirectly supported CO-1 by encouraging RA-35 and RA-36 to donate to CO-1." POA's letter then mentions the \$ payment from CO-29 that was credited to ORG. This was previously discussed under "20XX Expenses — Program Services".

POA's response referenced and included a fundraising letter from CO-1 Dean, DEAN-1, dated November 16, 20XX. Review of this letter showed this to be a general fundraising letter. It did not acknowledge past donations and did not solicit any specific amount for the future. The letter included information on the history of CO-1's CO-1 and provided statements as to why this was a worthy cause to support. POA's letter talks about this letter and then states *"It is disingenuous for CO-1 to argue that it was unaware of ORG's support or that ORG's support was not critical to its law school and programs.... When ORG prepared its Form 1023, ORG had every expectation that its support of CO-1 would be an integral part of CO-1's fundraising. In total, ORG gave \$\$ of direct and indirect cash contributions to CO-1 in 20XX and 20XX, and CO-1 acknowledged these contributions. Although \$\$ may not be an 'integral part' of CO-1's fundraising, it still is a significant sum of money and is consistent with ORG's charitable purpose of supporting CO-1."*

It should be noted that gross income received by ORG from during the audit years of 20XX through 20XX was approximately \$\$ (without regards to income received in 20XX from reimbursement of copied material for the LL.M. Program in Human Rights). The gross income received by ORG was calculated as follows:

TABLE DELETED

The only support provided to CO-1 since the inception of ORG was \$ of indirect support in 20XX and \$\$ direct support in 20XX. The \$ POA included in her calculation as paid to CO-1 was from CO-29. Total amount donated (\$\$) is less than % of the total gross receipts received by ORG.

The original acknowledgement for the donations from ORG to CO-1 was dated July 21, 20XX and was from the CO-1 CO-1's Assistant Dean, A-Dean. This acknowledgement was previously discussed and is included in the report as EXHIBIT J. A-Dean is no longer employed by CO-1 and was therefore unable to explain why a payment written from CO-29's account is credited to ORG. A third party contact was conducted to CO-1 in October 20XX to confirm the donations and to establish what support was provided by ORG to CO-1 from 20XX through the present^{ly} since ORG claims to be an entity providing support to CO-1. In CO-1's response, they acknowledged the donations listed on EXHIBIT J with the exception of the \$ check from CO-29. CO-1 did not verify any other support from ORG.

¹⁴ This was the series of donations discussed previously under "20XX Expenses – Program Services". See comments previously noted in the report and attached EXHIBIT D.

POA included a footnote that stated the following: *"Perhaps CO-1 is confused in its July 7, 20XX letter when it states that it was unaware that ORG was established as an organization*

set up to support the CO-1. Perhaps CO-1 thinks that the IRS is asking CO-1 to negate the idea that ORG is a section 509(a)(3) supporting organization for CO-1. Given that CO-1 has section 509(a)(3) supporting organizations, such as the Friend of CO-1 it is possible that CO-1 thinks that ORG is characterizing itself as a supporting 509(a)(3) supporting organization. As discussed in its Form 1023, ORG was created as a publicly supported charity under section 170(b)(1)(A)(vi). "

20XX Expenses — Unknown/Not Identified

Payment categorized as "Unknown — Not Identified" is for \$ wire transfer on 05/07/XX to "CO-62 Escrow — CO-33" per the wire transfer information. Initially it was believed this might be another donation to CO-33 which was discussed previously in tax year ending December 31, 20XX information. However, ORG's summary spreadsheet, identified the payment as "CO-63 — RA-41" and the comment "Wire Error — transfer out". To further confuse the understanding of this payment, POA provided some information on 07/10/20XX which included the following statement: "DIR-1 recalls that this relates to donors requesting a refund of their donations to ORG because ORG did not yet have its determination letter."

20XX Expenses — Investments

ORG purchased investments in the amount of \$\$ during 20XX. No investments were sold in 20XX. As discussed under the 20XX development, ORG provided information on its various investments. EXHIBIT Q is a recap of the investments for 20XX and 20XX. As reflected in the exhibit, investments included highly speculative investments in stocks including stocks privately held and stocks that traded over-the-counter (OTC). These investments ultimately resulted in overall loss to ORG.

¹⁵ Review of ORG's financial records indicate no payments to CO-1 in 20XX or 20XX.

LAW:

Internal Revenue Code (Code) Section 501(c)(3) provides that organizations that are "Corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, ... **no part of the net earnings of which inures to the benefit of any private shareholder or individual...**" (emphasis added) are exempt from Federal income tax under this section.

Federal Income Tax Regulation (Regulation) Section 1.501(c)(3)-1(a)(1) states: "In order to be exempt as an organization described in Section 501(c)(3), an organization **must be both organized and operated exclusively for one or more of the purposes specified in such Code section.** If an organization fails to meet either the organizational test or the operational test, it is not exempt." (emphasis added)

Regulation Section 1.501(c)(3)-1(c) defines the "**Operational test**". Regulation Section 1.501(c)(3)-1(c)(1) "Primary activities" provides, in part: "An organization will be regarded as '**operated exclusively**' for one or more exempt purposes **only if it engages primarily in**

activities which accomplish one or more of such exempt purposes specified in Section 501(c)(3). An organization will **not** be so regarded if **more than an insubstantial part** of its activities is not in furtherance of an exempt purpose." (emphasis added)

Regulation Section 1.501(c)(3)-1(c)(2) "Distribution of earnings" expands on the definition of an activity that is not in furtherance of an exempt purpose. It states: "An organization is **not operated exclusively for one or more exempt purposes if its net earnings inure in whole or in part to the benefit of private shareholders or individuals**. For the definition of the words 'private shareholder or individual', see paragraph (c) of Sec. 1.501(a)-1." (emphasis added)

Regulation Section 1.501(a)-1(c) defines 'private shareholder or individual' when it states: "The words 'private shareholder or individual' in Section 501 refer to persons having a personal and private interest in the activities of the organization."

Regulation Section 1.501(c)-1(d)(ii) provides emphasis to the operational test. It states that an organization is not organized or operated exclusively for one or more exempt purposes **"...unless it serves a public rather than a private interest**. Thus ... it is necessary for an organization to establish that it is not organized or operated for the benefit of private interests such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests." (emphasis added)

Revenue Ruling 77-366, 1977-2 C.B. 192, states that operating exclusively for charitable, religious, or educational purposes "has been construed as requiring all the resources of the organization to be applied to the pursuit of such purposes.

Revenue Ruling 56-304, 1956-2 C.B. 306, states that charitable organizations are not precluded from making distributions of their funds to individuals, provided such distributions are made on a true charitable basis in furtherance of the purposes for which they are organized. In addition, it should maintain adequate records and case histories to show the name and address of each recipient of aid, the amount distributed, the purpose for which the aid is given, the manner in which the recipient was selected and the relationship that exists between the recipient and members, officers, and trustees of the organization or a corporation controlled by the such individuals; in order to establish that distributions are made for charitable purposes.

In American Campaign Academy v. Commissioner, 92 T.C. 1053, (1989), the Court addressed the operational test and illuminates the difference between private benefit, derived by private interests where such private benefit is adverse to exemption under Section 501(c)(3), from inurement, derived by insiders, which also is adverse to exemption under Section 501(c)(3). It states:

"The Treasury Regulations specify three conditions which must be satisfied for an organization to meet the operational test. *Church by Mail, Inc. v. Commissioner*, 765 F.2d 1387, 1391 (9th Cir. 1985), affg. *T.C. Memo. 1984-349*. First, the organization must be primarily engaged in activities which accomplish one or more of the exempt purposes specified in Section 501(c)(3). *Sec. 1.501(c)(3)-1(c)(1), Income Tax Regs.* Second, the

organization's net earnings must not be distributed in whole or in part to the benefit of private shareholders or individuals. *Sec. 1.501(c)(3)-1(c)(2), Income Tax Regs.* Third, the organization must not be an "action" organization, i.e., one which devotes a substantial part of its activities attempting to influence legislation, or participates or intervenes, directly or indirectly, in any political campaign. *Sec. 1.501(c)(3)-1(c)(3), Income Tax Regs.*

...To establish that it operates primarily in activities which accomplish exempt purposes, petitioner must establish that no more than an insubstantial part of its activities does not further an exempt purpose. *Sec. 1.501(c)(3)-1(c)(1), Income Tax Regs.* The presence of a single substantial nonexempt purpose destroys the exemption regardless of the number or importance of the exempt purposes. *Better Business Bureau v. United States, 326 U.S. 279, 283 (1945); Copyright Clearance Center v. Commissioner, 79 T.C. 793, 804 (1982).*

... Prohibited private benefits may include an 'advantage; profit; fruit; privilege; gain; [or] interest.' *Retired Teachers Legal Fund v. Commissioner, 78 T.C. 280, 286 (1982).* Occasional economic benefits flowing to persons as an incidental consequence of an organization pursuing exempt charitable purposes will not generally constitute prohibited private benefits. *Kentucky Bar Foundation v. Commissioner, 78 T.C. at 926.* Thus, should petitioner be shown to benefit private interests, it will be deemed to further a nonexempt purpose under *Section 1.501(c)(3)-1(d)(1)(ii), Income Tax Regs.* This nonexempt purpose will prevent petitioner from operating primarily for exempt purposes absent a showing that no more than an insubstantial part of its activities further the private interests or any other nonexempt purposes. *Sec. 1.501(c)(3)-1(c)(1), Income Tax Regs.*

... We have consistently recognized that while the prohibitions against private inurement and private benefits share common and often overlapping elements, *Church of Ethereal Joy v. Commissioner, 83 T.C. 20, 21 (1984), Goldsboro Art League, Inc. v. Commissioner, 75 T.C. 337, 345 n. 10 (1980),* the two are distinct requirements which must independently be satisfied. *Canada v. Commissioner, 82 T.C. 973, 981 (1984); Aid to Artisans, Inc. v. Commissioner, 71 T.C. at 215.* Nonetheless, we have often observed that the prohibition against private inurement of net earnings appears redundant, since the inurement of earnings to an interested person or insider would constitute the conferral of a benefit inconsistent with operating exclusively for an exempt purpose. *Western Catholic Church v. Commissioner, 73 T.C. 196, 209 n. 27 (1979),* affd. in an unpublished opinion *631 F.2d 736 (7th Cir. 1980).* See also *sec. 1.501(c)(3)-1(c)(2), Income Tax Regs.* In other words, when an organization permits its net earnings to inure to the benefit of a private shareholder or individual, it transgresses the private inurement prohibition and operates for a nonexempt private purpose.

...The absence of private inurement of earnings to the benefit of a private shareholder or individual does not, however, establish that the organization is operated exclusively for exempt purposes. Therefore, while the private inurement prohibition may arguably be subsumed within the private benefit analysis of the operational test, the reverse is not true. Accordingly, when the Court concludes that no prohibited inurement of earnings exists, it cannot stop there but must inquire further and determine whether a prohibited private benefit is conferred. See *Aid to Artisans, Inc. v. Commissioner, 71 T.C. at 215; Retired Teachers Legal Fund v. Commissioner, 78 T.C. 280, 287 (1982).*

Moreover, an organization's conferral of benefits on disinterested persons may cause it to serve 'a private interest' within the meaning of *Section 1.501(c)(3)-1(d)(1)(ii), Income Tax Regs. Christian Stewardship Assistance, Inc. v. Commissioner, 70 T.C. 1037 (1978)*. See *Kentucky Bar Foundation v. Commissioner, supra; Aid to Artisans, Inc. v. Commissioner, supra*; see also *The Martin S. Ackerman Foundation v. Commissioner, T.C. Memo. 1986-365*. In this connection, we use "disinterested" to distinguish persons who are not private shareholders or individuals having a personal and private interest in the activities of the organization within the meaning of *Section 1.501(a)-1(c), Income Tax Regs. "*

In defining who is an insider, *United Cancer Council, Inc. v. Commissioner, 165 F. 3d 1173, 1176 (7th Cir. 1999)*, states: "The term "any private shareholder or individual" in the inurement clause of *Section 501(c)(3) of the Internal Revenue Code* has been interpreted to mean an insider of the charity. *Orange County Agricultural Society, Inc. v. Commissioner, 893 F.2d 529, 534 (2d Cir. 1990)*; *Church of Scientology v. Commissioner, supra, 823 F.2d at 1316-19*; *Church by Mail, Inc. v. Commissioner, 765 F.2d 1387, 1392 (9th Cir. 1985)*; *American Campaign Academy v. Commissioner, 92 T.C. 1053, 1066 (1989)*. A charity is not to siphon its earnings to its founder, or the members of its board, or their families, or anyone else fairly to be described as an insider, that is, as the equivalent of an owner or manager. The test is functional. It looks to the reality of control rather than to the insider's place in a formal table of organization. The insider could be a "mere" employee-- or even a nominal outsider, such as a physician with hospital privileges in a charitable hospital, *Harding Hospital, Inc. v. United States, 505 F. 2d 1068, 1078 (6th Cir. 1974)*..."

Revenue Ruling 69-383, 1969-2 CB 113, in examining the compensation arrangement between a radiologist and an exempt hospital wherein the radiologist was paid on the basis of a fixed percentage of the radiology department's income, provides criteria useful in distinguishing between an insider and private interests. It notes: "Under certain circumstances, the use of a method of compensation based upon a percentage of the income of an exempt organization can constitute inurement of net earnings to private individuals." The presence of a percentage compensation agreement will destroy an organization's exemption under *Section 501(c)(3) of the Code* "where such arrangement transforms the principal activity of the organization into a joint venture ... (*Lorain Avenue Clinic v. Commissioner, 31 T.C. 141 (1958)*), or is merely a device for distributing profits to persons in control (*Birmingham Business College v. Commissioner, 276 F. 2d 476 (1960)*)." The compensation agreement in this ruling did not constitute inurement because (1) the amount received was not excessive but was reasonable in terms of the responsibilities and activities the radiologist assumed under the contract, (2) the radiologist did not control the hospital and, (3) the compensation agreement was as a result of arms-length bargaining.

The Courts have determined that the inurement proscription does not prevent the payment of reasonable compensation for goods and services and the payment of reasonable salaries and benefits do not give rise to inurement. Though the Courts in *Mabee Petroleum Corp. v. United States, 203 F. 2d 872 (5th Cir. 1953)*; *Birmingham Business College, Inc. v. Commissioner, 276 F. 2d (476) (5th Cir. 1960)* determined that excessive salaries do result in inurement, they have, in addressing the issue, indicated that the payment of reasonable salaries by a tax-exempt organization does not result in the inurement of net earnings to the benefit of private individuals. See. In their decisions the Courts indicate that this

determination of whether the salaries paid are reasonable is a question of fact.

The Court in United Cancer Council v. Commissioner, 165 F. 3d 1173 (7th Cir. 1999) stated that the inurement provision of the Code "is designed to prevent the siphoning of charitable receipts to insiders of the charity, not to empower the IRS to monitor the terms of arm's length contracts made by charitable organizations with the firms that supply them essential inputs, whether premises, paper, computers, legal advice, or fundraising services."

In People of God Community v. Commissioner, 75 T.C. 127 (1980) the Court, in examining the compensation arrangement of an insider, noted that it is an established principle that the organization is entitled to pay reasonable compensation to an insider but the burden of establishing the reasonableness of the compensation fell upon the organization. It noted that where the insider's (Donhowe's) compensation was based "... upon a percentage of petitioner's gross receipts, apparently subject to no upper limit, a portion of petitioner's earnings is being passed on to Donhowe. See Birmingham Business College, Inc. v. Commissioner, 276 F.2d 476 (5th Cir. 1960), affg. on this point T.C. Memo. 1958-166; est of Hawaii v. Commissioner, 71 T.C. 1067 (1979), appeal filed (9th Cir., June 1, 1979); Founding Church of Scientology v. United States, 188 Ct. Cl. 490, 412 F.2d 1197 (1969), cert. denied 397 U.S. 1009 (1970). The statute specifically denies tax exemption where a portion of net earnings is paid to private shareholders or individuals. We hold here that paying over a portion of *gross* earnings to those vested with the control of a charitable organization constitutes private inurement as well. All in all, taking a slice off the top should be no less prohibited than a slice out of net."

The inurement of earning to an insider is described in Founding Church of Scientology v. United States, 412 F. 2d 1197 (Ct. Cl. 1969), cert. den., 397 U.S. 1009 (1970). The Court determined that the different arrangements between the organization and its founder, such as payment of ten percent or gross revenues, lending of money to him and his family, payment of expenses on their behalf, rental of property at inflated prices, resulted in inurement. The Court rejected the reasonable compensation defense. It stated: If in fact a loan or other payment in addition to salary is a disguised distribution or benefit from the net earnings, the character of the payment is not changed by the fact that the recipient's salary, if increased by the amount of the distribution or benefit, would still have been reasonable.

It is clear in other decisions that an organization's net earnings may inure to the benefit of private individuals in ways other than by the actual distribution of dividends or payment of excessive salaries. General Contractors' Ass'n v. United States, 202 F. 2d 633 (7th Cir. 1953) - reports and surveys furnished to members; Chattanooga Auto. Club v. Commissioner, 182 F. 2d 551 (6th Cir. 1950) - services to members; Underwriters' Laboratories, Inc. v. Commissioner, 135 F. 2d 371 (7th Cir.), cert. denied, 320 U.S. 756 (1943) - reports and studies furnished; Spokane Motorcycle Club v. United States, 222 F. Supp. 151 (E.D. Wash. 1963) - goods, services, and refreshments given. That the benefit conveyed may be relatively small does not change the basic fact of inurement. Spokane Motorcycle Club v. United States, supra.

Though inurement involves the flow of funds or other financial resources from the exempt organization to an individual that is an insider of the organization, the determination of private benefit does not require that payments for goods and services be unreasonable or exceed fair market value. In est of Hawaii v. Commissioner, 71 T.C. 1067 (1979) the Court upheld the revocation of the organization's exemption where it had operated for another organization that

exerted considerable control over it. In upholding the revocation, the Court stated "Nor can we agree with petitioner that the critical inquiry is whether the payments made to International were reasonable or excessive. Regardless of whether the payments made by petitioner to International were excessive, International and EST, Inc., benefited substantially from the operation of petitioner."

In a similar case, Westward Ho v. Commissioner, TCM 1992-192 (1992), the Court noted that the organization that had been created by three restaurant owners to provide funds to 'indigent and antisocial persons', thereby enabling them to leave the city, did in fact have another motive. It determined that the organization's true motive was to provide its creators with a more desirable business environment by removing disruptive homeless persons from the area. The court ruled that the organization did not qualify for exemption even though it provided direct 'assistance' to members of the charitable class.

In Church by Mail v. Commissioner, 765 F.2d 1387 (9th Cir. 1985) affg TCM 1984-349 (1984), the Court noted that Church by Mail, Inc. ('Church') paid Twentieth Century Advertising Agency ('Twentieth') for services provided. Twentieth was owned and controlled by the two individuals who ran Church. The Tax Court had found it unnecessary to consider the reasonableness of payments made by the applicant to a business owned by its officers. In addressing whether Church operated for a substantial non-exempt purpose the 9th Circuit Court of Appeals, in affirming the Tax Court's decision, stated: "... The critical inquiry is not whether particular contractual payments to a related for-profit organization are reasonable or excessive, but instead whether the entire enterprise is carried on in such a manner that the for-profit organization benefits substantially from the operation of the Church. *est of Hawaii v. Commissioner*, 71 T.C. at 1080-81; see also *Presbyterian & Reformed Publishing Co. v. Commissioner*, 743 F.2d 148, 155 (3d Cir. 1984) (courts must look to all objective indicia from which a corporate actor's intent may be discerned); *United States v. Dykema*, 666 F.2d 1096, 1100 (7th Cir. 1981), cert. denied, 456 U.S. 983, 72 L. Ed. 2d 861, 102 S. Ct. 2257 (1982) (it is necessary and proper for the I.R.S. to survey all of the activities of an organization to determine whether a non-exempt purpose is furthered). "

Code Section 6001, "Notice or Regulations Requiring Records, Statements, and Special Returns" provides, in part: "Every person...shall keep such records, render such statements, make such returns, and comply with such rules and regulations as the Secretary may from time to time prescribe."

Code Section 6033(a)(1) "Returns by Exempt Organizations" provides, in part: "Except as provided in paragraph (3), every organization exempt from taxation under 501(a) shall file an annual return, stating specifically the items of gross income, receipts, and disbursements, and such other information for the purpose of carrying out the internal revenue laws as the Secretary may by forms or regulations prescribe, and shall keep such records, render under oath such statements, make such other returns, and comply with such rules and regulations as the Secretary may from time to time prescribe...."

Code Section 6033(a)(3)(A) provide mandatory exceptions to the filing requirements under Code Section 6033(a)(1) including Code Section 6033(a)(3)(A)(ii) which states "any organization (other than a private foundation, as defined in Section 509(a) described in

subparagraph (C), the gross receipts of which in each taxable year are normally not more than \$5,000..."

As explained in Revenue Procedures 96-10, 1996-1 CB 577 the Internal Revenue Service has the authority to create discretionary exceptions to the requirement to file an annual information return if the filings of certain returns is not necessary to efficiently administer the internal revenue laws. As stated in Announcement 82-88, 1982-25 I.R.B. 23, the Service exercised this discretionary authority by expanding the filing exception to include Code Section 501(c) exempt organizations (other than private foundations) whose gross receipts in each tax year are not normally more than \$25,000 (thus expanding the \$5,000 limit in the statutory exception)

Regulations Section 1.6033-2(g)(1)(iii) "Organizations not required to file" includes "An organization (other than a private foundation) the gross receipts of which in each taxable year are normally not more than \$5,000 (as described in subparagraph (3) of this paragraph)..."

Regulations Section 1.6033-2(g)(3), as modified by Announcement 82-88, 1982-25 I.R.B. 23, provides "For purposes of subparagraph (1)(iii) of this paragraph, the gross receipts (as defined in subparagraph (4) of this paragraph) of an organization are normally not more than \$25,000 if — (i) In the case of an organization which has been in existence for one year or less, the organization has received, or donors have pledged to give, gross receipts of \$37,500 or less during the first taxable year of the organization, (ii) In the case of an organization which has been in existence for more than one but less than 3 years, the average of the gross receipts received by the organization in its first 2 taxable years is \$30,000 or less, and (iii) In the case of an organization which has been in existence for 3 years or more, the average of the gross receipts received by the organization in the immediately preceding 3 taxable years, including the year for which the return would be required to be filed, is \$25,000 or less.

Regulation Section 1.6033-2(i)(2) discusses returns filed by exempt organizations. Regulation Section 1.6033-2(i)(2) "Records, statements, and other returns of tax-exempt organizations" provides, in part: "Every organization which is exempt from tax, whether or not it is required to file an annual information return, shall submit such additional information as may be required by the Internal Revenue Service for the purpose of inquiring into its exempt status and administering the provisions of subchapter F (Section 501 and following), chapter 1 of subtitle A of the Code, Section 6033, and chapter 42 of subtitle D of the Code."

Revenue Ruling 59-95, 1959-1 C.B. 627 provides, in part: "failure or inability to file the required information return or otherwise to comply with the provision of section 6033 of the Code and the regulations which implement it, may result in the termination of the exempt status of an organization previously held exempt, on the grounds that the organization has not established that it is observing the conditions required for the continuation of an exempt status."

Internal Revenue Code (Code) Section 7602(a) provides the authority "to examine any books, papers, records, or other data which may be relevant or material" for the purpose of

ascertaining the correctness of any return....

IRC Section 162 states that ordinary and necessary expenses paid or incurred in carrying on a trade or business shall be allowed as a deduction.

IRC Section 274 addresses the disallowance of certain expenses. In Section 274(d) "Substantiation Required" provides that no deduction is allowed under Section 162 for any traveling expense (including meals and lodging while away from home); for any item with respect to an activity which is of a type generally entertainment, amusement, recreation, or use of the facility used in connection with such an activity; or for any gifts, unless the taxpayer substantiates by adequate records or by sufficient evidence corroborating the taxpayer's own statement- (a) the amount of the expense, (b) the time, place of travel, entertainment, amusement, recreation, or use of the facility or property, or the date and description of the gift (c) the business purpose of the expense or other item, (d) the business relationship to the taxpayer of the persons entertained, using the facility or property, or receiving the gift.

Regulation Section 1.274-5 addresses the substantiation requirements with respect to the business purpose of an expense. If the substantiation requirements are not met no deduction is allowed with respect to that expense.

Regulation Section 1.274-5T(b) identifies the elements that the taxpayer must substantiate with respect to the expenditure: (i) amount, (ii) time and place of travel, entertainment, amusement, recreation, or use of the facility or property, (iii) business purpose, and (iv) the business relationship to the taxpayer of each person entertained, using the facility or property, or receiving the gift. Section 1.274-5T(c) notes that a taxpayer must substantiate each element of an expenditure by adequate records or by sufficient evidence corroborating taxpayer's own statement. Section 274(d) contemplates that a taxpayer will maintain and produce such substantiation as will constitute clear proof of an expenditure referred to in Section 274. It states that a record of the elements of an expenditure made at or near the time of expenditure, supported by sufficient documentary evidence, has a high degree of credibility not present with respect to a statement prepared subsequent thereto when generally there is a lack of accurate recall. It states that the corroborative evidence required to support a statement not made at or near the time of the expenditure "must have a high degree of probative value to elevate such statement and evidence to the level of credibility reflected by a record made at or near the time of the expenditure supported by sufficient documentary evidence". It states that to obtain a deduction for travel, etc., a taxpayer must substantiate each element of the expenditure.

Regulations Section 1.274-5(c)(4)(i) defines an adequate account to an employer. Per this section, an "adequate accounting" means the submission to the employer of an account book, diary, log, statement of expense, trip sheet, or similar record maintained by the employee in which the information as to each element of an expenditure or use is recorded at or near the time of the expenditure or use, together with supporting documentary evidence, in a manner that conforms to all the adequate records requirements of this section.

IRC 3121(d)(1) provides that the term employee means "any officer of a corporation...".

Employment tax Regulation section 31.3121(d)-(1) provides regulations to define who is an employee. Section 31.3121(d)-1(a)(3) provides "If the relationship of employer and employee exists, the designation or description of the relationship by the parties as anything other than that of employer and employee is immaterial. Thus, if such relationship exists, it is of no consequence that the employee is designated as a partner, co-adventurer, agent, independent contractor, or the like."

Employment tax Regulation section 31.3121(d)-1(b) provides that corporate officers, generally, are employees of the corporation. "...However, an officer of a corporation who as such does not perform any services or performs only minor services and who neither receives nor is entitled to receive, directly or indirectly, any remuneration is considered not to be an employee of the corporation..."

GOVERNMENT'S POSITION:

ORG failed to operate as an organization exempt under Section 501(c)(3) of the Internal Revenue Code

The following is a timeline depicting events from the date of incorporation to the receipt of the determination letter:

Articles of
Inc. filed
02/13/XX

Form 1023
filed on
04/10/XX

Case Re- Est.
on 12/12/XX

Although certain activities were historical as shown in the table above, Form 1023 contained various inaccuracies or misstatements when compared to the actual activities including:

- ✓ Foundation will provide CO-1 LL.M. programs in Tax and Human Rights with contributions in order that the program will be able to provide support to their students.

Contributions to CO-1 are minimal compared to income received by the organization. Considerable payments were payments either made directly to or paid for the benefit of DIR-1 directly or indirectly.

- ✓ Foundation is viewed as an integral fundraising activity required by the LL.M. programs in order to continue their success.

CO-1 was unaware that that ORG was established to be an organization set up to support the CO-1. Also, ORG fundraising was not an integral fundraising activity required by the LL.M. programs or any other program at CO-1 as evidenced by the third party response from the University. CO-1 has stated that no contributions have been received from ORG since June 20XX.

- ✓ The Foundation will hold conferences, meetings, and assemblies to provide a forum for the discussion and dissemination of relevant information and data to promote a better understand of international, economic, tax and fiscal topics. The Foundation will sponsor at

least three conferences each year at CO-1 featuring such economic and fiscal topics.

CO-1 has stated in a third party response that there was no relationship between CO-1 and ORG with regards to the conferences; there are no contracts for such a purpose. The Form 1023 was signed under penalties of perjury. The penalty statement is directly above the signature

Assignment Agreement (Notice 20XX-81) Income Received 08/XX — 02/XX Ltr 947 issued granting exempt status on 05/10/XX (Effective 04/10/XX) Case Closed FTE on 11/13/XX line and states *"I declare under the penalties of perjury that I am authorized to sign this application on behalf of the above organization and that I have examined this application, including the accompanying schedules and attachments, and to the best of my knowledge it is true, correct, and complete."*

Conference materials provided and reviewed indicates that two conferences were held in 20XX, Country and City; one in 20XX, Cayman Island; and one in 20XX, City. ORG was not listed as a sponsor for any of these conferences. DIR-1 and DIR-2 were listed as either participants and/or presenters at the conferences. A review of the website for CO-29 shows that CO-29 sponsors the conferences. The Form 1023, Application for Recognition of Exemption was filed on April 10, 20XX. At that time, the conferences for Country and City had already been held. A review of the financial records reviewed indicated no conference expenses were paid in 20XX or 20XX; in 20XX some payments were made to DBA and CO-29 which may be related to conferences sponsored by CO-29 and not ORG.

✓ The Foundation will edit and publish papers, magazines, periodicals and books.

The Foundation holds no copyrights or editorial mention other than on its own website. Individuals are paid wages to edit and prepare articles that DIR-1 directs. Individuals interviewed with respect to certain activities have said that editing and writing are for DIR-1 and in some cases, editorial credit went to DIR-1.

NOTICE 20XX-81

As mentioned in the Facts Section, the IRS issued Notice 20XX-81 describing a transaction in which a taxpayer claims a loss upon the assignment of a section 1256 contract to a charity but fails to report the recognition of gain when the taxpayer's obligation under an offsetting non-section 1256 contract terminates. ORG was the recipient of assignment agreements to which the notice applied during the tax years ending December 31, 20XX and 20XX.

The assignment agreements were reported as charitable donations by ORG. The term donation is defined by Webster's Ninth New Collegiate Dictionary as "the action of making a gift esp. to a charity or public institution." ORG did send acknowledgment letters to the "donors." One hundred percent (100%) of the gross receipts reported by ORG in the year of incorporation was the result of the assignment agreement transaction. As a result of listing this transaction, the Service subsequently disallowed the contribution amounts on the Form 1040 of all the "contributors" in this sheltered transaction. It should be noted that in some instances the "contributor" did not take the contribution deduction on the return and they

self-reported their involvement. It should be further noted that there have been no more referrals of wealthy client from the asset management firms that have contributed to ORG.

Operations/Activities

DIR-1 has stated in interviews that he spends about 40 to 60 hours a month handling ORG matters and has done so for years while at the same time being a full-time professor for CO-1. Activities of CO-1 and CO-29 have been described as activities of ORG; however, a review of the financial information indicates differently.

✓ The check payable to CO-1 from the CO-29 was signed by DIR-1. This was reflected as a program service activity by ORG.

✓ Payment for services by employees of CO-1 that exceeded what was allowed to be paid by CO-1' policy

✓ Payment for services that were directed by DIR-1 paid by ORG when the payees did not know who or what ORG was

Income in the amount of \$ \$ (\$ in 20XX and \$ in 20XX) has been established to come from tax sheltered activity. Even though ORG received this sum from shelter activities, although reported differently, nominal amounts were spent for ORG's exempt purposes and a substantial amount was paid to or paid for the benefit of ORG's president/co-director, DIR-1.

For tax year ending December 31, 20XX, verification was provided that \$ was expended for the development of CO-1's LL.M. program in Human Rights.

For tax year ending December 31, 20XX, audit of the records indicate the following amounts were for program services:

- Grants/Allocations — \$ to CO-33; \$ to CO-1
- Research — \$ research grant paid to RA-20.

For tax year ending December 31, 20XX, audit of the records indicate the following amounts were for program services:

- \$ payment to CO-50 for the contract between ORG and CO-50 regarding the diploma agreement/publishing box on tax compliance.
- \$ CO-64; \$ City County Recorder
- \$\$ to CO-1
- \$ paid to CO-52 for business expenses

Under IRC section 162, in general, there shall be allowed as a deduction, all the ordinary and necessary expenses paid or incurred during the taxable year in carrying out any trade or business. What is not allowed are expenses paid on behalf of a third party; CO-1 or CO-29. In addition, as a professor at university, it is reasonable that DIR-1 in his position as a professor would have educational expenses, but this does not allow him to use assets of a public charity for his own benefit.

In addition, there has been a misclassification of payments for services rendered as research grants. ORG does not have a formal grant policy. ORG did not comply with even the most basic recordkeeping requirements with respect to grants or other distributions to individuals. See Rev. Rul. 56-304. ORG was unable to demonstrate that the payments to individuals were based on any charitable criteria or demonstrate that the recipients of the distributions

were members of a charitable class. Students by definition are not a charitable class.

Per Rev. Rul. 56-304, 1956-2 C.B. 306, provides that an organization is not precluded from section 501(c)(3) exemption when it makes grants to individuals, provided the distributions are made on a true charitable basis and in furtherance of its exempt purposes. Such organizations should keep adequate records and case histories to show the name and address of the recipients of aid; the amount distributed to each; the purpose for which the aid was given; the manner in which the recipient was selected; and the relationship, if any, between the recipient and (1) members, officers, or trustees of the organization, (2) a grantor or substantial contributor to the organization or a member of the family of either; and (3) a corporation controlled by a grantor or substantial contributor.

As previously mentioned, there was a problem with respect to ORG's records due to . ORG's address of record is in City and that is the area that was impacted by the hurricane. DIR-1 was physically located in State, both his residence and office. Although he stated that he spent 40 to 60 hours per month on ORG's matters, the records lost were retained in the City area. The individuals who were compensated for services rendered performed these services in the State office. This office was also the office of the LL.M. Program of CO-1.

Payment made to or for President/Director DIR-1 constitutes private benefit/inurement

As mentioned above, although ORG received \$\$ (\$ in 20XX and \$ in 20XX) in what has been established to come from tax sheltered activity and ORG received \$ from IBLs in 20XX, although reported differently, nominal amounts were spent for ORG's exempt purposes and a substantial amount was paid to or paid for the benefit of ORG's president/co-director, DIR-1.

Some payments were reported as research grants; however, a review of financial and third party information reveal that most payments were for services rendered. These services were directed by DIR-1 or were for the benefit of DIR-1. In some cases the services were payments that the University would not pay.

As a professor at CO-1 and as Director of the LL.M. program in International Taxation, DIR-1 has a vested interest in making the LL.M. program appear to be highly successful. This benefits him directly by assuring him of job security, increases in pay and job promotions. To limit costs CO-1 was paying, and to make the program look more successful, DIR-1 had some of the costs paid for by ORG which was a benefit to him. Although the costs may have some elements of being educational support in nature, the true end result was to promote DIR-1 in his position as Director of the LL.M. program.

Payment made to family members of President/Director DIR-1 constitutes private benefit/inurement

Payments were made to President/Co-Director's DIR-1 sister and her husband, RA-30 and RA-2, during November 20XX. These payments were reported as expenses on the Form 990. In response to IDRs asking for documentation to verify these expenses contracts were

provided for both RA-30 and RA-2. These contracts were mentioned in the previous section of this report. It should be further noted that both the contracts:

- were dated November 20, 20XX;
- were three year contracts;
- were not to commence until January 1, 20XX; and
- were paid upfront in 20XX.

RA-30's was a "Contract for Services Agreement" which called for fundraising, administrative and consulting services. No fundraising materials were submitted to reflect the fundraising activities that were undertaken. The bank summonsed bank records do not reflect any deposits for contributions, gifts or grants. Per a statement submitted by the POA on DIR-1 behalf, he did not directly contact any of the donors prior to their contributions to ORG. He did personally contact asset managers who represented wealthy individuals as a means of soliciting charitable contributions for ORG. No W-2 or 1099 was issued by ORG for the \$ that was paid. This amount was not reported as income, by her own statement, until an amended Form 1040 was filed in July, 20XX.

RA-2 is an attorney by profession. The documentation for his payment was a retainer agreement. The agreement states that RA-2 would deduct \$ per month for administrative services and would deduct at a rate of \$ per hour for legal and consulting services rendered during the agreement period. If the retainer were exhausted prior to the expiration of the agreement, ORG would pay additional funds in increments of \$.

During the May 2, 20XX interview previously mentioned, RA-2 stated that his administrative services included handling the paperwork and other information for ORG that was sent to the address of record, Address, City, State. RA-2 stated that he expended 3 hours per month for this activity. Specifically, he stated that letters and bank statements were sent to that address and he would put the information/statements in a folder and then mail to DIR-1 in City. DIR-1, after reviewing in City, would then re-mail the items to his accountant in City, State. This activity occurred, and ORG was billed, even after caused an interruption in mail service in the City area from August 29, 20XX until regular mail service was resumed on April 3, 20XX. In addition, although RA-2's three-year contract was dated November 20, 20XX and was effective January 1, 20XX, State Secretary of State records revealed attorney RA-1 was the registered agent of ORG from February 13, 20XX until RA-2 was appointed on April 7, 20XX. The official address of record was DIR-1's place of business. There were no payments to DIR-1 per review of the financial records.

A review of the summonsed bank records for 20XX revealed a second \$ payment to RA-2 was made via Check # on January 6, 20XX. This amount was not reflected in his billing records. When the payment was questioned, the response was that it was another retainer for professional services to establish an unrelated organization. This statement does not excuse or explain the non-reporting of substantial income received by attorney RA-2 and the failure to timely file an amended return, Form 1040X, to include the income received by RA-2 and RA-30.

It should also be noted that both the RA-2s were being paid per the contract or retainer

agreement for "administrative services." Fiduciary responsibility notwithstanding, with respect to the contracts, ORG failed to properly report the contracts in their books and records and on the 20XX Form 990. ORG failed to provide W-2s and or 1099s for these individuals. The individuals, by their own admission, failed to report the payments.

The same date payments were made to RA-2 and RA-30, November 30, 20XX, ORG made a \$ contribution to CO-33, the 501(c)(3) organization that is run by President/Co-Director DIR-1 mother, DIR-5.

In DIR-5 response, she stated "Since the \$ was placed in the operating account one could argue that family received some of the money because family members were employees of CO-33." During the formal interview held with DIR-1 on February 7, 20XX, information was obtained that DIR-1's Form 1040 for 20XX was amended to include \$ from CO-33. The Form 990s for CO-33 for 20XX, 20XX and 20XX reflected compensation to RA-2 (\$, \$, \$ respectively) and compensation to DIR-5 of \$ in 20XX and \$ in 20XX for their positions as directors of CO-33 Since CO-33 was not audited, is unknown how much, if any, payments were made RA-30.

In addition to the \$ donation to CO-33, the charity run by DIR-5, on January 5, 20XX, a check was written to DIR-5 in the amount of \$. This represented a three year up-front contract for rent. The rent is for the office space for ORG located at Address, City, State. The space has been described as the room above the garage. DIR-5 resides at Address. As stated previously, ORG did not provide verification that a physical office specifically for ORG activities actually existed nor did they establish that it was ordinary and necessary under IRC § 162 when minimal activities may be conducted there. The Service does not challenge that the State Secretary of State may require a domicile in State for a corporation. However, prior to April 7, 20XX, ORG used the registered agent's (RA-1's) business address of Address City, State as ORG's domicile address and used the former POA's (POA's) address of Address, City State for ORG's mailing address.

In summary, the only individuals to receive full payment in advance for three-year contracts were family members; mother, sister, and brother-in-law. Payments in amount of \$\$ and the \$ contribution were made on the same date. The \$ to DIR-5 and the second \$ to RA-2 and were made by consecutive checks # to DIR-5 on 01/05/20XX and # to RA-2 on 01/06/20XX.

ORG failed to file employment tax returns.

Audit findings indicate that either Form W-2, Wage and Tax Statement, or Form 1099-MISC, Miscellaneous Income, should have been issued to the employees and/or independent contractors. The applicable forms were not filed and the proper withholding amounts were not submitted to the Service.

ORG failed to accurately prepare Form 990, Return of Organization Exempt From Income for the tax year ending December 31, 20XX through tax year ending December 31, 20XX.

The following are some of discrepancies noted during this examination:

- ORG reported "contributions" of \$ on the Form 990 for the period ending December 31, 20XX. The Service has determined that these amounts were from tax shelter transactions reported on Notice 20XX-81 and the Service has disallowed the contribution amounts on the Form 1040 of all participants (contributors) in the sheltered transactions. The donors in this situation had no charitable intent.
- A bank account analysis reflected more deposited into the CO-30 account in 20XX than was reported on the Form 990.
- The financial records reflected there were two wire transfer payments of \$ each to the law firm CO-32. The bank statement reflected one of the payments was reversed on 09/27/20XX with the comment "Book credit for ORG...Rev of our dbt to yr acct 09/20/XX..." ORG incorrectly claimed \$ more in legal expense in 20XX than actually paid.
- ORG claims they were paying for and sponsoring conferences, but there was no verification provided that these conferences were sponsored by ORG. The conference materials provided indicated the entity who was the sponsor, CO-29 (CO-29), was not a tax-exempt organization, but DIR-1 and DIR-2 were both members of the CO-29.
- CO-33 is a 501(c)(3) exempt organization that is run by DIR-5. DIR-5 is the mother of DIR-1 and she was also the Compliance Officer of ORG. RA-2 is the brother-in-law to Williams DIR-1 and he was also the Secretary of ORG. The Form 990 for ORG for all years under audit reflected Donee's Relationship as "None".
- ORG submitted minutes indicating DIR-6 was a member of ORG's Board of Directors in 20XX. DIR-6 is the director of the L.L.M. Program in Human Rights at CO-1. During a third party contact with DIR-6, he stated he was not a Board of Director member and had never been a board member or an officer of ORG. DIR-6 was not listed on the 20XX Form 990 as a director or officer.
- ORG claimed charitable donations to CO-1 in 20XX of \$. A third party request to CO-1 resulted in the presentation of Check # for \$ dated 07/01/20XX payable to "CO-1" from CO-29. This payment was not made by ORG and therefore cannot be shown on the Form 990 as Program Service expense of the organization.
- ORG is claiming that the materials used in the L.L.M. Program in International Taxation are the property of ORG. However, the L.L.M. Program was established back in 19XX at CO-18 CO-1 (City) and the materials used in the course are from materials published by Dorothy and RA-35.
- Payments categorized as "Loans" during the audit were checks that included the annotation of a loan in the memo line of the check. There were no loans reflected on ORG's balance sheet.
- The payments to various individuals were for services rendered rather than "educational research" as noted on the Form 990 or as "research grants" as noted on the checks.
- Payments were made to or for the benefit of RA-24 totaling over \$\$\$. This included payments directly to RA-27 as well as payments for a rental vehicle and the dormitory at CO-1. RA-27's statement indicated services were for DIR-1. POA's submitted a response indicating RA-27 was traveling from City to State to present his findings and no lodging was provided.
- RA-30 and RA-2 (sister and brother-in-law to president/co-director DIR-1) were both paid per the contract or retainer agreement for "administrative services." Fiduciary

responsibility notwithstanding, with respect to the contracts, ORG failed to properly report the contracts in their books and records and on the 20XX Form 990. ORG failed to provide W-2s and or 1099s for these individuals. The individuals, by their own admission, failed to report the payments.

- The Form 990 for Tax Year Ending December 31, 20XX was submitted to the Service with all blanks and the Block K was checked indicating there was no filing requirements due to the "organization's gross receipts are normally not more than \$." This was determined to not be true since the summonsed bank records indicated \$ deposited from one source and the average gross receipts for 20XX, 20XX and 20XX were substantially more than \$.
- In conducting the compliance check, ORG has not filed its Form 990 for Tax Years Ending December 31, 20XX or December 31, 20XX. POA previously informed the auditor that ORG was looking into whether or not they have a filing requirement since their gross receipts maybe be less than \$. Discussion was held that pursuant to IRC §6033 and the applicable regulations, the gross receipt filing requirement is an average \$ over a rolling three-year period and the bank information for Tax Years Ending December 31, 20XX through December 31, 20XX clearly reflects an average above the \$. In addition, based on information provided by POA concerning the sales of investment, ORG had gross receipts from the sale of the investments in excess of \$.

TAXPAYER'S POSITION:

After the facts were shared with ORG, a written response was submitted "outlining and discussing the items with the greatest impact on ORG's tax-exempt status and which it most strongly disagrees." This included the following:

- 1) "Alleged Private Inurement to DIR-1" – ORG does not believe the amount paid to or for the benefit of DIR-1 constitutes private inurement because "DIR-1 has repaid over \$ to reimburse it for loans and advances that he received."

Government's Response: In reviewing the timeline on the examination, ORG was notified in early May 20XX of the commencement of the examination. At that time, only a small amount of the amounts paid to or for the benefit of DIR-1 was repaid. The repaying of such a substantial amount after the notification of examination supports the government's position that ORG was not operated for a substantial exempt purpose, but was set up to benefit DIR-1.

- 2) "ORG's Alleged Participation in Major-Minor Transactions Described in Notice 20XX-81" – ORG points out that DIR-1's relationship with CO-10 "occurred in 20XX and 20XX *before* the formation of ORG". In addition, "ORG fails to see the relevance of any correspondence between DIR-1' and CO-10 that occurred prior to the formation of ORG and was about matters completely unrelated to operating a charitable organization".

Government's Response: This is discussed above under the Facts and under Government Position. As a summary, in order for the Notice 20XX-81 transactions to occur, the promoter (CO-10) needed to have an accommodating charity. From the records reviewed, ORG was the charity used to foster these transactions. It is possible DIR-1

specifically set-up ORG to be used for this promotion since all the income received and reported in tax year 20XX was from the sheltered transactions and, for tax year 20XX, substantial income was received and deposited into ORG's bank account from the sheltered transactions, but not reported on the Form 990. Per review of the financial records for the audit years, the only contribution received by ORG was \$ from FAC-2 who DIR-1 acknowledged was a colleague and co-worker at CO-1. The government does not believe that ORG was properly operated as a charitable organization

3) "Expense Reimbursements to DIR-1" — ORG is maintaining the expenses were "not personal expenses of DIR-1 and they served the legitimate business purpose of ORG" and "are ordinary and necessary business expenses of ORG."

Government's Response: ORG has not been able to establish to the satisfaction of the government that it is operating for an exempt purpose. DIR-1 was the full-time director of the International Tax LL.M. program at CO-1, City, State which is the university that ORG was established to support. As such, even though paying some of the expense may have somewhat indirectly benefited the university, the payments directly benefited DIR-1 and the programs he was involved in. By having an outside organization, in this case ORG, pay for some expenses directly related to the LL.M. program it gave CO-1 the impression that the program was more success than it was. The International Tax LL.M. program was ended at CO-1 around the end of 20XX and, based on information received from CO-1 in November 20XX, the CO-1' last support received from ORG was in June 20XX.

4) "ORG's Charitable Activities" — ORG is maintaining they are operating for a charitable purpose.

Government's Response: The lack of a charitable purpose is discussed extensively throughout this report and is summarized in the Government's Position. The government does acknowledge that ORG paid for course materials for CO-1's Human Rights LL.M. program and the amount paid out for the materials was reimbursed by the students who participated in the Human Rights program. There was no giving of funds directly to the Human Rights program to allow that program to use the funds as deem necessary; there was no provision to cover the costs for students unable to pay for the materials; etc. Although DIR-1 used ORG's funds to pay students/researchers to assist in the International Tax LL.M. program that he was the director or and responsible for, and DIR-1 paid for meetings and dinners relating to activities relating to his International Taxation LL.M. program, this did not occur when assisting other areas of CO-1, including the assistance provided to the Human Rights LL.M. program. The difference being, by supporting the International Taxation LL.M. program of which DIR-1 was the Director, DIR-1 was indirectly supporting and benefiting himself.

5) "ORG's Payments to Individuals" — ORG is maintaining these payments are in furtherance of its exempt purpose. ORG explains the payments to family members are reasonable and necessary. ORG position on the payment to non-family members was for the purpose of loans which have now been substantially repaid and payment to individuals for "falls within ORG's charitable purpose of editing and publishing papers,

magazines, pamphlets, periodicals and books."

Government's Response: Much of this section is devoted to discussing the payments to DIR-1' family members. This is extensively addressed in Government's Position above. The payments to individuals were substantially for the benefit of DIR-1.

SUMMARY:

ORG is not in compliance with the filing requirements under IRC §6033. The Form 990s for Tax Year Ending December 31, 20XX and Tax Year Ending December 31, 20XX have a filing requirement, have not been filed and are considered delinquent.

Based on the examination of records, interviews and third party information, revocation is proposed effective the date of incorporation, February 20XX. Contributions to ORG are no longer deductible as charitable contributions. Any contributions to this organization by those who were in part responsible for, or were aware of, the activities or deficiencies on the part of the organization that gave rise to loss of exempt status should not be allowed as a deduction.

ORG will be required to file Form 1120 for all years since inception.

If this proposed revocation becomes final, appropriate State officials will be advised of the action in accordance with Internal Revenue Code Section 6104(c) and applicable regulations.